(29,475)

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1922.

No. 925.

CLALLAM COUNTY, WASHINGTON; WILLIAM A. NELSON, SHERIFF OF CLALLAM COUNTY, WASHINGTON; E. C. STEWART, TREASURER OF CLALLAM COUNTY, WASHINGTON, ET AL.

vs.

THE UNITED STATES OF AMERICA AND UNITED STATES SPRUCE PRODUCTION CORPORATION.

ON CERTIFICATE FROM THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT.

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JUDD & DETWEILER (INC.), PRINTERS, WASHINGTON, D. C., APRIL 10, 1923.

1 **UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT.**

No. 3938.

CLALLAM COUNTY, WASHINGTON, WILLIAM A. NELSON, Sheriff of Clallam County, Washington; E. C. Stewart, Treasurer of Clallam County, Washington, and J. O. Morse, Assessor of Clallam County, Washington, Appellants,

vs.

THE UNITED STATES OF AMERICA and UNITED STATES SPRUCE PRODUCTION CORPORATION, a Corporation, Appellees.

Upon Appeal from the United States District Court for the Western District of Washington, Northern Division.

Certificate of the United States Circuit Court of Appeals for the Ninth Circuit Certifying Certain Questions or Propositions of Law to the Supreme Court of the United States under Section 239, Judicial Code.

Before Gilbert, Morrow, and Rudkin, Judges.

This suit was brought in the United States District Court for the Western District of Washington, Northern Division, by the United States Spruce Production Corporation, a corporation incorporated under the laws of the State of Washington, and the United
2 States, as parties plaintiff, against Clallam County, a municipal corporation of the State of Washington, and the taxing officers of said county, all citizens of the State of Washington, defendants, for a decree cancelling taxes levied by said county and state for the years 1919, 1920 and 1921, upon physical properties, to wit, a logging railroad, saw mill, timber lands and other physical properties, legal title to which was, during the years for which taxes were so levied, in the said United States Spruce Production Corporation.

On hearing in the District Court a decree was entered, maintaining jurisdiction in said District Court and holding the property exempt from state and county taxes and permanently enjoining the collection of the taxes complained of.

From this decree an appeal was perfected and prosecuted to the United States Circuit Court of Appeals for the Ninth Circuit. The appeal was presented on written briefs and oral argument. At the close of the oral argument the said Court of Appeals, desiring the instructions of the Supreme Court of the United States for proper decision on certain questions or propositions of law, ordered that such a certificate be prepared and filed.

Statement of Necessary Facts to be Considered in Connection with the Questions Propounded.

The United States, acting under authority contained in the Acts of Congress of June 3, 1916, March 4, 1917, July 24, 1917,
3 and April 11, 1918, as amended by Act of July 9, 1918, had, prior to August 21, 1918, entered into a contract with the Siems-Carey—H. S. Kerbaugh Corporation to construct a logging railroad, build a saw mill, acquire rights of way, timber and timber lands in Clallam County, State of Washington, for the production of air craft for use of the United States in the World War.

On August 21, 1918, the Director of Air Craft Production of the United States, acting under the authority of the Act of Congress of July 9, 1918, caused four civilians and three army officers to prepare, execute and acknowledge articles of incorporation of the plaintiff, Spruce Corporation, conforming to the laws of the State of Washington, and caused such articles to be filed with the proper state and county officers of the State of Washington, paying the required fees and taking all necessary steps to complete the incorporation of such corporation under the laws of said state.

Although the original articles of incorporation gave the corporation very broad powers, these articles were amended to confine the powers of the corporation to those prescribed by Act of Congress authorizing the creation of the corporation. This was done at a special meeting of the board of trustees, October 23, 1918, and a special meeting of the stockholders, November 1, 1918, at which all of the stock was represented in person or by proxy. The change was in conformity with the suggestion of the Advocate General.

The capital stock was ten million dollars and was subscribed as follows:

The United States subscribed for 99,993 shares, and each of the seven trustees subscribed for one share. The trustees' shares
4 being at once assigned to the United States so that the United States at all times owned or controlled all the capital stock.

At the time of the trial Lieutenant-Colonel Charles Van Way, President, and Lieutenant Colonel Arthur L. Fuller, Comptroller and Treasurer of the corporation, were army officers assigned to duty with the corporation by the War Department, and they drew their compensation from the treasury of the United States. Each held one share of stock and served as trustee of the corporation. The third member of the board, who also held one share, was Charles H. Carey, a civilian.

These persons each signed a waiver in the following form:

"For value received, I hereby assign and set over to the Secretary of War of the United States of America, or to his order for the benefit of the United States of America, any and all moneys, property or dividends which are now due me or which may hereafter become due me or accrue to me from any source whatsoever by reason of any stock in United States Spruce Production Corporation, a Washing-

ton corporation. It is understood that the share of stock now standing in my name on the books of the corporation has been issued to me solely for the purpose of qualifying me as a trustee of said corporation."

These trustees of the corporation endorsed their shares in blank and turned them back to the secretary. Certificate No. 8 was, upon organization of the corporation, issued to the Director of Aircraft Production of the United States for 99,993 shares. At the time this certificate was issued, the number of trustees as provided by the articles of incorporation was seven. Thereafter the number of trustees was reduced by amendment of the articles to three; whereupon four shares which were held by the outgoing trustees were
5 issued on certificate No. 17 to the Director of Aircraft Production of the United States. The certificates were in the hands of the Director of Aircraft Production, lodged for safekeeping with the Chief of Finance of the United States. The physical custody of the qualifying shares held by the three trustees is in the Secretary of the United States Spruce Production Corporation.

At the time the corporation was organized the logging railroad and mill had been partially completed under the Siems-Carey-Kerbaugh contract, and timber, mill site and rights of way acquired.

Thereupon, on October 10, 1918, the United States assigned the Siems-Kerbaugh contract to the corporation, and conveyed to the corporation by bargain and sale deed all lands and property now sought to be taxed by Clallam County. This deed contains no restrictions or limitations, the conveying clause being as follows:

"The United States of America, represented by the Secretary of War acting through the Director of Air craft Production, the Grantor, has bargained, sold, assigned, transferred and conveyed and set over, and by these presents does bargain, sell, assign, transfer, convey and set over unto said United States Spruce Production Corporation, the Grantee, and its successors and assigns, the following described property."

And the habendum clause is as follows:

"To have and to hold all and singular the above described property, contracts, rights and privileges to the said grantee, its successors and assigns, forever."

The consideration recited is "of the sum of $274,164.76 paid to the United States, the receipt whereof is hereby acknowledged,
6 and of the assumption by the grantee of all outstanding debts and obligations of the United States of America incurred through the operation of the Spruce Production Division and the Bureau of Air Craft Production."

At the time the corporation was created the United States conveyed to the corporation all of its aeroplane properties and activities. The corporation's activities were wholly directed to the government's program of production of aeroplane lumber.

The Spruce Corporation thereupon issued its bonds or debentures aggregating twenty five million dollars. The United States paid on its stock subscription $100,000 and purchased twenty-five million dollars of the Spruce Corporation's bonds, ten million of which were taken in payment of the property so transferred and conveyed as above set forth; for the remaining fifteen million, credit for a working capital was given the Spruce Corporation by the United States.

In creating the corporation, the Director of Air Craft Production directed, and the trustees of the corporation authorized, the issuance of debentures to the amount of $25,000,000. These were issued and were delivered to the Register, therein named, for the United States. By their provisions they are to be retired by liquidation of the corporation, and they bear 5 per cent interest if such interest is earned by the corporation; they are payable out of the net assets of the corporation and shall not be payable unless a sum sufficient after liquidation is accumulated to retire them. Originally it was contemplated that the Allied Governments were to take debentures as well as the United States, but this was not done, as Potter, the acting
7 Director of Aircraft Production, did not accept this suggestion of his subordinate and that plan was never carried out. No debenture was ever sold, none was issued to any other government, and all that were taken and held by the United States were taken in exchange for cash or its equivalent in the land and other properties conveyed by the Secretary of War to the corporation. They are all to be repaid out of liquidation by the terms of the debentures.

The Spruce Corporation then functioned as a State of Washington corporation, and continued the completion of the logging railroad, mill and the acquisition of necessary materials for manufacture of air-craft for the use of the United States in the World War, prosecuting such work until the armistice. After the armistice its activities have been directed to liquidating its affairs and in this connection, it, for a recited consideration, bought and sold timber, entered into contracts for use of its logging railroad, one contract covering a period of ten years, and another two years, the Spruce Corporation to receive stipulated payments for use of its road as follows:

There was some timber down on the right of way and two contracts were entered into with C. J. Erickson with respect to cleaning up the down timber.

There was also a contract with the Puget Sound Mills and Timber Company, February, 1921. This contract covered a period of ten years and contemplated transactions affecting the railroad. It provided for a method whereby the title to this property could be perfected and put in salable condition, and provided for the hauling of logs of the timber company over the railroad during a period
8 of ten years in exchange for deeds. A considerable amount of right of way acquired by the corporation itself was acquired from the Puget Sound Mill and Timber Company, and this contract covered that transaction. The land was necessary as an integral part of the Spruce Production railroad, a considerable part of it.

These were all the contracts relating to hauling products over this road.

The corporation also entered into a contract with Clallam Lumber Company for the purchase of logs, in the latter part of 1920. The contention was made by the Clallam Lumber Company that an isolated body of timber at the western terminus of this Spruce railroad No. 1 was made valueless to them by reason of the ownership of the railroad. And in the settlement of the various claims, both on the part of the Spruce Production Corporation and the Clallam Lumber Company the price was set upon this timber, which included some 6,000,000 feet, and it was taken over by the corporation. The corporation, as a part of the same transaction, secured from the Clallam Lumber Company a release of claims which had been prosecuted by that company against the corporation. The price paid the Clallam Timber Company was three dollars per thousand for that timber, and after holding it a few months, the corporation sold it to Erickson for five dollars for all species other than hemlock, and two dollars for hemlock. This contract resulted in a complete clearance of title for the western terminus of the railroad, which was part of the lands acquired by the corporation under its activities, the title to which was not perfected until this contract was entered into.

9 The railroad in question is 36 miles long with a right of way 100 feet wide and the mill site covers approximately 100 acres, all situated in Clallam County, Washington.

The Spruce Corporation employed both civilians and soldiers. It was licensed and authorized to transact business in the State of Washington, and had in all respects complied with the laws of that state entitled it to transact business in said state. It was organized and incorporated under the laws of the State of Washington, and is a citizen of that state, and has been conducted and operated as a private business corporation organized under the laws of the State of Washington.

In May, 1918, the President, by virtue of the power conferred upon him by the so-called Overman Act, created the Bureau of Air Craft Production and a Division of Military Aeronautics, the executive officer of which was made the Director of Air Craft Production.

On January 29, 1919, subsequent to the Armistice, these two divisions were placed together, forming the Air Service, as then provided for by Army Regulations, functioning under the Director of Air Service, whose title was subsequently (July 11, 1919) changed to Chief of Air Service by Act of Congress approved on that date. This Air Service, with its powers, functions and duties, as then provided by orders and Army Regulations, continued until June 30, 1920, on which date the National Defense Act, Amended, came into effect and provided for the office of Chief of Air Service. Army Regulation No. 95-5 November 17, 1921, Paragraph E. as prescribed by the Chief of Air Service, is as follows:

"I will in accordance with instructions from the Secretary
10 of War, exercise administrative supervision over the liquidation of the Bureau of Air Craft Production and the United States Spruce Production Corporation."

The United States never advanced directly any money to the Spruce Corporation, but subscribed for its stock and purchased its bonds as above stated, and the corporation was financed solely by money paid by the United States on its stock subscription and for the bonds.

The legal title to and possession of the property assessed for state and county taxes and involved in this suit, during the period for which taxes were assessed, has been in the Spruce Corporation.

The Spruce Corporation has never declared any dividends. At the time of the trial it owed the United States on bonds purchased $5,338,667.09 and the $100,000 paid by the United States on its stock subscription. It owed current debts, $28,482.49 and had assets of book value, $11,953,904.57.

The operations of the corporation as a whole show loss, and the total liquidation of all the remaining assets will not be equivalent to the total amount expended.

The questions of law concerning which the Circuit Court of Appeals of the Ninth Circuit desires the instruction of the Supreme Court of the United States are:

I.

Did the United States District Court have jurisdiction of the suit?

II.

Is the property held by the Spruce Corporation under the above statement of facts, subject to state taxation?

WM. B. GILBERT,
WM. W. MORROW,
FR. H. RUDKIN,
Judges of the United States Circuit Court of Appeals for the Ninth Circuit.

11 [Endorsed:] Certificate of the United States Circuit Court of Appeals for the Ninth Circuit, Certifying Certain Questions or propositions of law to the Supreme Court of the United States under section 239 Judicial Code. Filed March 5, 1923, F. D. Monckton, Clerk, By Paul P. O'Brien, Deputy Clerk.

A true copy.

Attest March 10, 1923.

[Seal of United States Circuit Court of Appeals, Ninth Circuit.]

F. D. MONCKTON,
Clerk,
By PAUL P. O'BRIEN,
Deputy Clerk.

12 [Endorsed:] No. 3938. United States Circuit Court of Appeals for the Ninth Circuit. Clallam County, Washington, et al., Appellants, vs. The United States of America, et al., Appellees. Certified Copy of Certificate of the United States Circuit Court of Appeals for the Ninth Circuit, Certifying Certain Questions or Propositions of Law to the Supreme Court of the United States under Section 239 Judicial Code.

Endorsed on cover: File No. 29,475. U. S. Circuit Court of Appeals, Ninth Circuit. Term No. 925. Clallam County, Washington; William A. Nelson, sheriff of Clallam County, Washington; E. C. Stewart, treasurer of Clallam County, Washington, et al. vs. The United States of America and United States Spruce Production Corporation. Filed March 26th, 1923. File No. 29,475.

Supreme Court of the United States

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Supreme Court of the United States

CLALLAM COUNTY, WASHINGTON;
WILLIAM A. NELSON, Sheriff of Clallam County, Washington,
E. C. STEWART, Treasurer of Clallam County, Washington, and
J. A. MORSE, Assessor of Clallam County, Washington,
Appellants,

vs.

THE UNITED STATES OF AMERICA, and UNITED STATES SPRUCE PRODUCTION CORPORATION, a Corporation,
Appellees.

No._____

UPON CERTIFICATE FROM THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

APPELLANTS' BRIEF

STATEMENT

This cause comes to this Court from the United States Circuit Court of Appeals for the Ninth Circuit, on certificate certifying certain questions or propositions of law to this Court under section 239, Judicial Code. The certificate is as follows (omitting the caption):

"Upon Appeal from the United States District Court for the District of Washington. (No. 3938).

Certificate of the United States Circuit Court of Appeals for the Ninth Circuit, certifying certain questions or propositions of law to the Supreme Court of the United States under Section 239, Judicial Code.

Before GILBERT, MORROW and RUDKIN, Judges.

This suit was brought in the United States District Court for the Western District of Washington, Northern Division, by the United States Spruce Production Corporation, a corporation incorporated under the laws of the State of Washington, and the United States, as parties plaintiff, against Clallam County, a municipal corporation of the State of Washington, and the taxing officers of said county, all citizens of the State of Washington, defendants, for a decree cancelling taxes levied by said county and state for the years 1919, 1920 and 1921, upon physical properties, to-wit, a logging railroad, saw mill, timber lands and other physical properties, legal title to which was, during the years for which taxes were

so levied, in the said United States Spruce Production Corporation.

On hearing in the District Court a decree was entered, maintaining jurisdiction in said District Court and holding the property exempt from state and county taxes and permanently enjoining the collection of the taxes complained of.

From this decree an appeal was perfected and prosecuted to the United States Circuit Court of Appeals for the Ninth Circuit. The appeal was presented on written briefs and oral argument. At the close of the oral argument the said Court of Appeals, desiring the instructions of the Supreme Court of the United States for proper decision on certain questions or propositions of law, ordered that such a certificate be prepared and filed.

Statement of Necessary Facts to Be Considered In Connection With the Questions Propounded.

The United States, acting under authority contained in the Acts of Congress of June 3, 1916, March 4, 1917, July 24, 1917, and April 11, 1918, as amended by Act of July 9, 1918, had, prior to August 21, 1918, entered into a contract with the Sims-Carey-H. S. Kerbaugh Corporation to construct a logging railroad, build a saw mill, acquire rights-of-way, timber and timber lands in Clallam County, State of Washington, for the production of air craft for use of the United States in the World War.

On August 21, 1918, the Director of Air Craft Production of the United States, acting under the authority of the Act of Congress of July 9, 1918, caused four civilians and three army officers to prepare, execute and acknowledge articles of incorporation of the plaintiff, Spruce Corporation, conforming to the laws of the State of Washington, and caused such articles to be filled with the proper state and county officers of the State of Washington, paying the required fees and taking all necessary steps to complete the incorporation of such corporation under the laws of said state.

Although the original articles of incorporation gave the corporation very broad powers, these articles were amended to confine the powers of the corporation to those prescribed by Act of Congress authorizing the creation of the corporation. This was done at a special meeting of the board of trustees, October 23, 1918, and a special meeting of the stockholders, November 1, 1918, at which all of the stock was represented in person or by proxy. The change was in conformity with the suggestion of the Advocate General.

The capital stock was ten million dollars and was subscribed as follows:

The United States subscribed for 99,993 shares, and each of the seven trustees subscribed for one share. The trustees' shares being at once assigned to the United Stats so that the United States at all times owned or controlled all the capital stock.

At the time of the trial Lieutenant-Colonel Charles Van Way, President, and Lieutenant Colonel Arthur L. Fuller, Comptroller and Treasurer of the corporation, were army officers assigned to duty with the corporation by the War Department, and they drew their compensation from the treasury of the United States. Each held one share of stock and served as trustees of the corporation. The third member of the board, who also held one share, was Charles H. Carey, a civilian.

These persons each signed a waiver in the following form:

> "For value received, I hereby assign and set over to the Secretary of War of the United States of America, or to his order for the benefit of the United States of America, any and all moneys, property or dividends which are now due me or which may hereafter become due me or accrue to me from any source whatsoever by reason of any stock in United States Spruce Production Corporation, a Washington corporation. It is understood that the share of stock now standing in my name on the books of the corporation has been issued to me solely for the purpose of qualifying me as a trustee of said corporation."

These trustees of the corporation endorsed their shares in blank and turned them back to the secretary. Certificate No. 8 was, upon organization of the corporation, issued to the director of Aircraft Production of the United States for 99,993 shares. At the time this certificate was issued, the number of trustees as provided by the articles of incorporation was seven. Thereafter the

number of trustees was reduced by amendment of the articles to three; whereupon four shares which were held by the outgoing trustees were issued on certificate No. 17 to the Director of Aircraft Production of the United States. The certificates were in the hands of the Director of Aircraft Production, lodged for safekeeping with the Chief of Finance of the United States. The physical custody of the qualifying shares held by the three trustees is in the Secretary of the United States Spruce Production Corporation.

At the time the corporation was organized the logging railroad and mill had been partially completed under the Siems-Carey-Kerbaugh contract, and timber, mill site and rights of way acquired.

Thereupon, on October 10, 1918, the United States assigned the Siems-Kerbaugh contract to the corporation, and conveyed to the corporation by bargain and sale deed all lands and property now sought to be taxed by Clallam County. This deed contains no restrictions or limitations, the conveying clause being as follows:

"The United States of America, represented by the Secretary of War acting through the Director of Aircraft Production, the Grantor, has bargained, sold, assigned, transferred and conveyed and set over, and by these presents does bargain, sell, assign, transfer, convey and set over unto said United States Spruce Production Corporation, the Grantee, and its successors and assigns, the following described property."

And the habendum clause is as follows:

"TO HAVE AND TO HOLD all and singular the above described property, contracts, rights and privileges to the said grantee, its successors and assigns, forever."

The consideration recited is "of the sum of $274,164.76 paid to the United States, the receipt whereof is hereby acknowledged, and of the assumption by the grantee of all outstanding debts and obligations of the United States of America incurred through the operation of the Spruce Production Division and the Bureau of Air Craft Production."

At the time the corporation was created the United States conveyed to the corporation all of its aeroplane properties and activities. The corporation's activities were wholly directed to the government's program of production of aeroplane lumber.

The Spruce Corporation thereupon issued its bonds or debentures aggregating twenty-five million dollars. The United States paid on its stock subscription $100,000 and purchased twenty-five million dollars of the Spruce Corporation's bonds, ten million of which were taken in payment of the property so transferred and conveyed as above set forth; for the remaining fifteen millions, credit for a working capital was given the Spruce Corporation by the United States.

In creating the corporation, the Director of Air Craft Production directed, and the trustees of the cor-

poration authorized, the issuance of debentures to the amount of $25,000,000. These were issued and were delivered to the Registrar, therein named, for the United States. By their provisions they are to be retired by liquidation of the corporation, and they bear 5 per cent interest if such interest is earned by the corporation; they are payable out of the net assets of the corporation and shall not be payable unless a sum sufficient after liquidation is accumulated to retire them. Originally it was contemplated that the Allied Governments were to take debentures as well as the United States, but this was not done, as Potter, the acting Director of Aircraft Production, did not accept this suggestion of his subordinate and that plan was never carried out. No debenture was ever sold, none was issued to any government, and all that were taken and held by the United States were taken in exchange for cash or its equivalent in the land and other properties conveyed by the Secretary of War to the corporation. They are all to be repaid out of liquidation by the terms of the debentures.

The Spruce Corporation then functioned as a State of Washington corporation, and continued the completion of the logging railroad, mill and the acquisition of necessary materials for manufacture of air-craft for the use of the United States in the World War, prosecuting such work until the armistice. After the armistice its activities have been directed to liquidating its affairs and in this connection, it, for a recited consideration, bought and sold timber, entered into contracts for use of

its logging railroad, one contract covering a period of ten years, and another two years, the Spruce Corporation to receive stipulated payments for use of its road as follows:

There was some timber down on the right of way and two contracts were entered into with C J. Erickson with respect to cleaning up the down timber.

There was also a contract with the Puget Sound Mills and Timber Company, February, 1921. This contract covered a period of ten years and contemplated transactions affecting the railroad. It provided for a method whereby the title to this property could be perfected and put in salable condition, and provided for the hauling of logs of the timber company over the railroad during a period of ten years in exchange for deeds. A considerable amount of right of way acquired by the corporation itself was acquired from the Puget Sound Mill and Timber Company, and this contract covered that transaction. The land was necessary as an integral part of the Spruce Production railroad, a considerable part of it.

These were all the contracts relating to hauling products over this road.

The corporation also entered into a contract with Clallam Lumber Company for the purchase of logs, in the latter part of 1920. The contention was made by the Clallam Lumber Company that an isolated body of

timber at the western terminus of this Spruce Railroad No 1 was made valueless to them by reason of the ownership of the railroad. And in the settlement of the various claims, both on the part of the Spruce Production Corporation and the Clallam Lumber Company the price was set upon this timber, which included some 6,000,000 feet, and it was taken over by the corporation. The corporation, as a part of the same transaction, secured from the Clallam Lumber Company a release of claims which had been prosecuted by that company against the corporation. The price paid the Clallam Timber Company was three dollars per thousand for that timber, and after holding it a few months, the corporation sold it to Erickson for five dollars for all species other than hemlock, and two dollars for hemlock. This contract resulted in a complete clearance of title for the western terminus of the railroad, which was part of the lands acquired by the corporation under its activities, the title to which was not perfected until this contract was entered into.

The railroad in question is 36 miles long with a right of way 100 feet wide and the mill site covers approximately 100 acres, all situated in Clallam County, Washington.

The Spruce Corporation employed both civilians and soldiers. It was licensed and authorized to transact business in the State of Washington, and had in all respects complied with the laws of that state entitled it

to transact business in said state. It was organized and incorporated under the laws of the State of Washington, and is a citizen of this state, and has been conducted and operated as a private business corporation organized under the laws of the State of Washington.

In May, 1918, the President, by virtue of the power conferred upon him by the so-called Overman Act, created the Bureau of Aircraft Production and a Division of Military Aeronautics, the executive officer of which was made the Director of Aircraft Production.

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"I will, in accordance with instructions from the Secretary of War, exercise administrative supervision over the liquidation of the Bureau of Aircraft Production and the United States Spruce Production Corporation."

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The questions of law concerning which the Circuit Court of Appeals of the Ninth Circuit desires the instruction of the Supreme Court of the United States are:

I.

Did the United States District Court have jurisdiction of the suit?

II.

Is the property held by the Spruce Corporation under the above statement of facts subject to state taxation?

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Judges of the United States Circuit Court of Appeals for the Ninth Circuit."

ARGUMENT.

QUESTION I.

Did the United States District Court have jurisdiction of the suit?

1. The United States is neither a necessary or proper party to this suit.

The interest of the United States in the Spruce Corporation is merely that of a stock and bond holder, and the United States is neither a necessary or proper party to litigation by or against the Spruce Corporation, or involving its property.

Bank of U. S. v. Planters Bank of Georgia,
6 L. Ed. (U. S.) 244.

Judge Marshall in the above case says:

"Many states of the Union which have an interest in banks are not sueable even in their own

courts. * * * As a member of a corporation the government never exercises its sovereignty. It acts merely as a corporator and exercises no other power in the management of the affairs of the corporation than are expressly given by the incorporation act."

(That is, by the laws of the State of Washington.)

The above case also holds that suits by or against The Bank of the United States in which the United States owned stock, were not suits against the United States.

Hawes v. Oakland, 26 L. E. (U. S.) 827, holds that a stockholder cannot maintain an action without showing that he "has exhausted all means within his reach to obtain within the corporation its redress of his grievance." (P. 832).

To the same effect, *Equity Rule* No. 27.

Jellenik v. Mining Co., 44 L. Ed. (U. S.) 647, holds:

"As the domicile of the company is and must be in the state that created it, the property represented by its certificates of stock may be deemed to be held by the company within the state whose creature it is whenever it is sought by suit to determine who is its real awner." (P. 651).

Barrow Steamship Co. v. Kane, 42 L. Ed. (U. S.) 964, holds:

"There is a *conclusive* presumption of law that the persons composing the corporation are citizens of the same state with the corporation." (P. 966).

So, in the case at bar, the United States, a stockholder, is *conclusively* presumed for jurisdictional purposes, to be a citizen of the State of Washington.

Fitzgerald v. Mo. Poc. Ry. Co., 45 Fed Rep., 812, holds a corporation is amenable to the laws of the state creating it. (P. 815).

> "The owner of all the stock and bonds of a corporation does not own the corporate property. The corporate property which includes all rights of action and claims for damages, belongs to the corporation and is subject to the management and control of its board of directors and if it be conceded that the defendant owns all the stock and bonds of the Denver Company, that fact gives it no title to or interest in the right-of-way or other property of that company, which it can make the basis of an action or plea in its own behalf." (Pp. 818-819).

This case also holds that in case of doubtful jurisdiction, jurisdiction should be refused.

In re Greenleaf, 56 N. E. (Ill.), 295, the court says:

> "That tangible property of the corporation and the shares of stock therein are separate and distinct kinds of property and belong to different owners—the first being the property of the artificial person, the corporation; the latter the property of the individual owner thereof,"

and holds that the shares of stock may be taxed in one jurisdiction and the physical property in another.

The Spruce Corporation is a separate entity and a citizen of the State of Washington. It is bound by its

contracts and is capable of suing and being sued. Its property can be subjected to execution. If its property is threatened by execution or wrongful seizure, the United States would have no standing to sue for injunction. The fact that the State or Clallam County are threatening to seize the property for taxes does not change the situation. It neither makes the United States a necessary or proper party nor involves the construction of any law of the United States.

See

U. S. v. Strang, 254 U S. 491; 65 L. Ed. 368.

Sloan Ship Yards Corporation, Astoria Marine Iron Works v. U. S. Shipping Board Emergency Fleet Corp., and *Fleet Corporation v. Wood, Trustee in Bankruptcy,* 257 U. S. p.—; 66 L. Ed. (U. S.) p.—.

The Ninth Circuit, in the recent case of *U. S. v. Mathews,* (Fed. Rep. Adv. Sheets, Vol. 282, No. 1, Oct. 6, 1922, p. 266), decided that the United States has not sufficient interest to maintain a suit to recover money paid out by the Fleet Corporation, hence it would seem that it could not join in a suit for the purpose of giving Federal Court jurisdiction.

In the late case from the Third Circuit, of *Manufacturers L. & I. Co. v. United States S. B. E. Fleet Corporation* (Advance Sheets Federal Reporter, Vol 284, page 231), the Court holds that a suit is maintainable against the Fleet Corporation; that it and not the

United States is the real party defendant. The Court also holds (page 236) that the Fleet Corporation having requistioned the fee of certain lands, that such lands "then belonged absolutely to the Fleet Corporation."

2. *This cause does not arise under the laws of the United States in the sense that a Federal Court would have jurisdiction.*

The constitution is in no way involved nor is a *construction* of any law of the United States involved. The Acts of Congress, pleaded in the complaint, their meaning and purposes as claimed, are not put in issue.

The sole question raised is one of fact as to the ownership of the properties taxed. There is no sound reason to have this question of fact presented to a Federal Court.

If a Federal Law is involved, it is only as it may tend to prove this fact of ownership. No disputed construction is involved.

The source of the money that bought the stock and bonds, the activities of the United States Officers, the activities of the Spruce Corporation, are all facts and involve no construction of Federal Law.

Blackburn v. Mining Co., 44 L. E. (U. S.), p. 276. holds that the application of the Federal statute must not only be involved, "but that the controversy was determined by a *construction* put upon the statute adverse

to the contention of one of the parties." (P. 283). That there must be a denial of right arising out of the construction of a Federal Statute.

To the same effect see

Shoshone Mining Co. v. Reutter, 44 L. Ed. (U. S.) 864;

Western Union Tel. Co. v. Ry. Co., 44 L. Ed (U. S.) 1052;

Little York Gold W. W. Co. v. Keyes, 24 L. Ed (U. S.) 656;

Bankers, etc., Co. v. Minneapolis, etc., R. Co., 48 L. Ed. (U. S.) 484.

In the *Fitzgerald* case, *supra* (45 Fed. Rep., 812) the court says (on page 819):

> "If there is no dispute between the parties as to the meaning of the Act of Congress, there is no Federal controversy between them and no cause for removal. The Supreme Court has settled the rule on this subject."

In the case of *Arkansas v. Choctaw, etc., R. Co.,* 134 Fed., 106, it is held that any doubt must be resolved against the jurisdiction and quotes from Judge Brewer as follows:

> "When a proposition has once been decided by the Supreme Court, it can no longer be said that in it there still remains a Federal question."

The Ninth Circuit has also held the same doctrine in the case of *Montana Ore Producing Company v. Boston, etc., Mining Co.*, 85 Fed., 867.

In the case of *Miller v. Illinois Central R. Co.*, 168 Fed., 982, on page 987, the court says:

> "It does not appear that a construction of the act known as the 'Employers Liability Act' of Congress is in any way involved in this case. It seems to be a case where the decision will depend entirely upon the facts of the case as applied to the law The mere application of an act of Congress to a case gives no right of removal."

The Spruce Corporation is a creature of the laws of the State of Washington—a citizen of that state. No constitutional question or construction of Federal law is involved. The United States is not a proper party plaintiff. On what principle can a Federal Court have jurisdiction?

In *Head & Armory v. The Provident Ins. Co.*, (2 Cranch, 127), Chief Justice Marshall said:

> "A state corporation is a creature of state law. Its qualities and disabilities are 'what the incorporating act has made it—to derive all its powers from that act, and to be capable of exerting its faculties only in the manner which that act authorizes. To this source of its being, then, we must recur to ascertain its powers."

In the *Dartmouth College* case (4 Wheaton, 636), it is said:

"Being a mere creature of the law, it possesses only those properties which the charter of its creation confers upon it."

In the *Dandridge* case (12 Wheaton, 64), it is said:

"Corporations created by statute must depend both for their powers and the mode of exercising them upon the true construction of the statute itself."

In the *Earle* case (13 Peters, 519, opinion, 587), Chief Justice Taney said:

"A state corporation can do no acts 'except such as are authorized by its charter; and those acts must also be done by such officers or agents, and in such manner as the charter authorizes.'"

And on page 588:

"It is very true that a corporation can have no legal existence out of the boundaries of the sovereignty by which it is created. It exists only in contemplation of law, and by force of the law; and when that law ceases to operate, and is no longer obligatory, the corporation can have no existence. It must dwell in the place of its creation, and cannot migrate to another sovereignty."

The acts of this corporation must be done by its officers and agents and in the manner authorized and prescribed by the laws of Washington. The fact that it confined, if it did confine, its activities to furthering the interests and purposes of its dominant stockholder, the United States, would not change the law; such acts are the acts of a creature of state law and are governed and limited by that law.

How is it permissable for this creature of state law, this citizen of the State of Washington, to be singled out from other citizens of Washington as a class by itself, and be allowed to present its controversies to a Federal Court?

Why should such a citizen be relieved from the obligations imposed by the same law on other citizens to support the state administration that gives its property protection?

The incorporation laws of the State of Washington are full and complete.

Remington's 1915 *Code,* Sec. 3677 and following.

Superior Courts of the State of Washington have jurisdiction of suits involving "title to real estate, or the legality of any tax."

Rem. 1015 *Code,* Sec. 15.

Suits to enjoin tax collection must allege and prove tender of taxes justly due.

Rem. Code, 1915, Sec. 955.

The State Board of Taxing Commissioners have "general supervision of the system of taxation throughout the state," with very broad powers.

Rem. Code, 1915, Sec. 9084, and following.

All property in the State of Washington is subject to taxation.

Rem. Code, 1915, Sec. 9091.

Suits by a state corporation must allege and prove payment of last annual license fee to the State.

Rem. Code, 1915, Sec. 3715.

If the Spruce Corporation engages in bazardous work it is subject to the *State Workmen's Compensation Law,* and must pay the State a percentage of its pay roll.

Rem. Code, 1915, Sec. 6604, and following.

If it operates its railroad as a common carrier it is subject to and governed by the *Public Service Commission Law* of the State of Washington.

Rem. Code, 1915, Secs. 8626-1 and following.

QUESTION II.

Is the property held by the Spruce Corporation, under the facts set forth in the certificate, subject to state taxation?

1. *Exemption from State Taxation of a Federal Agency can only arise by necessary implication or by express Congressional declaration.*

Such necessary implication depends not upon the fact of the agency, but upon the character and *necessary*

effect of the tax. From a tax which deprives the agent of the power to serve the Government, or directly and necessarily obstructs the exercise of that power, there is a necessary implication of exemption. From any other tax there is no such implication of exemption.

The tax upon the operation or right to function of the agent has the necessary effect of destroying or obstructing the power of the agent to serve, hence is impliedly prohibited. A tax upon the local property of the agent has no such necessary effect, hence is not impliedly prohibited and the exemption, if any, must arise from express Congressional declaration. This distinction runs through all the decisions.

McCulloch v. Maryland (4 Wheat., 316; 4 Law Ed., 579-600-609) is the leading case. It involved a stamp tax on notes issued by the Maryland branch of the old United States Bank, a corporation created by act of Congress. The Maryland law sought to prohibit the issuance of such notes except upon stamps for which must be paid to the state a graduated tax according to the denomination of the notes, and to prohibit the issuance of such notes except in specified denominations, not prescribed by the act of Congress creating the bank. The Federal Supreme Court, speaking through Chief Justice Marshall, held in substance that this was an attempt to tax the operations of the bank and to control or impede its right to function, as a governmental agency, and that the Maryland law was therefore unconstitutional and void. In his final summary Chief Justice Marshall said:

"This opinion does not deprive the states of any resources which they originally possessed. It does not extend to a tax paid by the real property of the bank, in common with the other real property within the state, nor to a tax imposed on the interest which the citizens of Maryland may hold in this institution, in common with other property of the same description throughout the state. But this is a tax on the operation of an instrument employed by the Government of the Union to carry its powers into execution. Such a tax must be unconstitutional."

Osborn v. Bank of United States, 9 Wheat., 738-867; 6 Law Ed., 204-235, involved a law of the State of Ohio imposing upon each office of discount and deposit of the Bank of the United States within that state an annual occupation tax of $50,000. The Court, again speaking through Chief Justice Marshall, held in substance, that the capacity of discount and deposit were essential to the operation of the bank and that therefore the exemption from a state tax on these operations, though not expressed by the Act of Congress, was necessarily implied. Noticing the alleged resemblance between the bank and a governmental contractor, Chief Justice Marshall said:

"Can a contractor, for supplying a military post with provisions, be restrained from making purchases within any state, or from transporting the provisions to the place at which the troops were stationed, or could he be fined or taxed for doing so? We have not yet heard these questions answered in the affirmative. It is true, that the property of the contractor may be taxed as the property of other citizens; and so may the local property of the bank. But we do not admit that the act of purchasing, or of

conveying the articles purchased, can be under state control,."

This language clearly recognizes the distinction upon which we insist, namely, between a tax upon the property of a governmental agent and a tax upon the action or right to function of such agent. This distinction, as said by Justice Strong in the *Peniston* case, "has ever since been recognized."

Thompson v. Union Pacific R. Co., 9 Wall., 579; 19 Law Ed., 792-798, was a suit to enjoin a state tax on the railroad's property. The railroad was incorporated by the Territorial Legislature and State Legislature of Kansas. Chief Justice Chase reviews prior decisions and finds in substance that exemption from state taxation of corporations employed as governmental agencies have been sustained in two classes of cases: (1) where the corporation was created under act of Congress and the tax was sought to be imposed on its operations or right to function, as in *McCulloch v. Maryland,* and, (2) where the act under which the corporation was formed expressly exempted the corporation or its property from state taxation or limited such taxation, as in *Bradley v. People,* 4 Wall., 459; 18 L. Ed., 433. He says:

> "But we are not aware of any case in which the real estate, or other property of a corporation not organized under act of Congress, has been held to be exempt, in the absence of express legislation to that effect, to just contribution, in common with other property, to the general expenditure for the common

benefit, because of the employment of the corporation in the service of the government."

He adds:

"We do not think ourselves warranted, therefore, in extending the exemption established by the case of *McCulloch v. Maryland,* beyond its terms. We cannot apply it to the case of a corporation deriving its existence from state law, exercising its franchise under state law, and holding its property within state jurisdiction and under state protection.

"We do not doubt the propriety or the necessity, under the Constitution, of maintaining the supremacy of the General Government within the constitutional sphere. We fully recognize the soundness of the doctrine, that no state has a 'right to tax the means employed by the Government of the Union for the execution of its powers.' But we think there is a clear distinction between the means employed by the government and the property of agents employed by the government. Taxation of the agency is taxation of the means; taxation of the property of the agent is not always, or generally, taxation of the means.

"No one questions that the power to tax all property, business and persons, within their respective limits, is original in the states, and has never been surrendered. It cannot be so used, indeed, as to defeat or hinder the operations of the National Government; but it will be safe to conclude, in general, in reference to persons and state corporations employed in government service, that when Congress has not interposed to protect their property from state taxation, such taxation is not obnoxious to that objection.

"Lane County v. Oregon (*ante,* 105); *Bank v. "Kentucky* (*ante,* 701).

"We perceive no limits to the principle of exemption which complainants seek to establish. It would remove from the reach of state taxation all the property of every agent of the Government. Every corporation engaged in the transportation of mails, or of government property of any description, by land or water, or in supplying materials for the use of the government, or in performing any service of whatever kind, might claim the benefit of the exemption. The amount of property now held by such corporations, and having relations more or less direct to the National Government and its service, is very great. And this amount is continually increasing; so that it may admit of question whether the whole income of the property which will remain liable to state taxation if the principle contended for is admitted and applied in its fullest extent, may not ultimately be found inadequate to the support of the state governments."

Union Pacific R R. Co. v. Peniston, 18-Wall., 5-50; 21 Law Ed., 787-791, was also a suit to enjoin a state tax on the property of the railroad in the state. The railroad corporation was created by Congress, as an agent of the general government, designed to be employed and actually employed in the service of the government, both military and postal. It was aided by a land grant and bonds advanced to it by the government, and the government expressly had the right to name five of its directors. The Court said:

"That the taxing power of a state is one of the attributes of sovereignty; that it exists independent-

ly of the Constitution of the United States, and underived from that instrument; and that it may be exercised to an unlimited extent upon all property, trades, business and avocations existing or carried on within the territorial boundaries of the state, except so far as it has been surrendered to the Federal Government, *either expressly or by necessary implication*, are propositions that have often been asserted by this court. And in thus acknowledging the extent of the power to tax belonging to the states, we have declared that it is indispensable to their continued existence." (Italics ours.)

After reviewing the *Thompson* case the Court said:

"It may, therefore, be considered as settled that no constitutional implications prohibit a state tax upon the property of an agent of the government merely because it is the property of such agent. A contrary doctrine would greatly embarrass the states in the collection of their necessary revenue without any corresponding advantage to the United States. A very large proportion of the property within the states is employed in execution of the powers of the government. It belongs to governmental agents, and is not only used, but is necessary for their agencies. United States mails, troops and munitions of war are carried upon almost every railroad; telegraph lines are employed in the national service. So are steamboats, horses, stage coaches, foundries, ship-yards, and multitudes of manufacturing establishments. They are the property of natural persons, or of corporations, who are instruments or agents of the General Government, and they are the hands by which the objects of the government are attained. Were they exempt from liability to contribute to the revenue of the state it is manifest the state governments would be paralyzed.

While it is of the utmost importance that all the powers vested by the Constitution of the United States in the General Government should be preserved in full efficiency, and while recent events have called for the most unembarrassed exercise of many of those powers, it has never been decided that state taxation of such property is impliedly prohibited."

Referring to *McCulloch v. Maryland* the Court said:

"The institution was prohibited from issuing notes at all except upon stamped paper furnished by the state, and to be paid for on delivery, the stamp upon each note being proportioned to its denomination. The tax, therefore, was not upon any property of the bank, but upon one of its operations; in fact, upon its right to exist as created. It was a direct impediment in the way of a governmental operation performed through the bank as an agent. It was a very different thing, both in nature and its effect, from a tax on the property of the bank. No wonder, then, that it was held illegal. But even in that case the court carefully limited the effect of the decision."

The court thus makes plain the distinction upon which we insist here, namely, a tax on the operations or right to function is prohibited by necessary implication; but a tax on the local property of the corporate agency is not prohibited by implication. It follows that such a tax can only be prohibited by express declaration of Congress. The court said:

"This distinction, so clearly drawn in the earlier decisions, between a tax on the property of a governmental agent, and a tax upon the action of such

agent, or upon his right to be, has ever since been recognized."

The court further said:

"It is, therefore, manifest that exemption of Federal agencies from state taxation is dependent, not upon the nature of the agents, or upon the mode of their constitution, or upon the fact that they are agents, but upon the effect of the tax; that is, upon the question whether the tax does in truth deprive them of the power to serve the government as they were intended to serve it, or does hinder the efficient exercise of their power. A tax upon their property has no such necessary effect. It leave them free to discharge the duties they have undertaken to perform. A tax upon their operations is a direct obstruction to the exercise of Federal powers."

Justice Field dissented in this *Peniston* case, but in the next case which we shall notice he receded from his former position and said: "But on further consideration I have come to the conclusion that the rule laid down in the *Thompson case* is the true and sound rule."

County of Santa Clara v. Southern Pacific R. Co., 18-Fed., 385, involved county taxes levied upon the franchises and property of the defendant railroad corporations formed under the laws of the State of California. Two of these companies, with consent of the Legislature of California, were selected as special agents of the Federal Government and received grants of power and privileges from the Federal Government as postal and military roads, not possible under the original organization. They contended that the power to tax their fran-

chises involved the power to destroy the companies and urged that the tax was therefore void.

The opinion was written by Justice Field. Following the rule in the *Thompson case* he said:

> "The state, it is conceded, cannot use its taxing power so as to defeat or burden the operation of the general government. And when the government has itself created the instrumentality used, its exemption from a state taxation necessarily follows. But we are of the opinion yielding to the decision cited, that when the instrumentality is the creation of the state,—a corporation formed under its laws,—and is employed or adopted by the general government for its convenience, although to enlarge its use and render it more available additional privileges and benefits are conferred by the government upon the corporation, it remains subject to the taxing power of the state, unless Congress declares it to be exempt from such power. Congress can undoubtedly exempt any agencies it may employ for services to the general government from such taxation as will in its judgment impede or prevent their performance. Occasions may arise hereafter, especially in time of war, where the necessities of the Federal Government will require such exemption of the roads of the companies, and of their franchises and appurtenances, to be declared, and enforced; the exemption to continue until the necessities calling for it shall cease. But as yet Congress has not declared any such exemption either of their property or of their franchises, and we therefore think that none exists."

The above language is directly applicable here. The Spruce Corporation is organized under the laws of the

State of Washington. Therefore, "it remains subject to the taxing power of the State, unless Congress declares it exempt from such power." This is especially true where, as here, the tax is purely a property tax and not a tax on the franchise.

Central Pacific Railroad Co. v. California, 162 U. S., 91-128; 40 Law Ed., 903-915, involved the validity of a tax on the railroad's franchise included in its return with its other property for taxation. The railroad company was organized under the laws of the State of California and derived its franchise from those laws. It appeared also that it had as an agency of the Federal Government an additional franchise from the Federal Government. It was contended that the whole tax was void in that it included a tax on the Federal franchise which was exempt from State taxation. The Court, speaking through Chief Justice Fuller, held that the State franchise was not exempt from taxation, and that in the absence of a showing to the contrary the franchise taxed was presumed to be that which the State could legally tax, namely, the State franchise and not the Federal franchise. The tax was held valid.

Choctaw, Oklahoma & Gulf R. Co. v. Mackey, (U. S. Supreme Court Adv. Opinions No. 16, July 1st, 1921, p. 639) is the most recent expression of the Supreme Court of the United States on this question of state taxation of property of Federal agencies. The railroad there in question served certain coal mines situated upon lands

leased from the Choctaw Indians and it was conceded that the railroad was used by the Government as an agency in carrying out its policy toward the Indians. The Court, following the rule in the *Peniston* and other cases, held the state tax on the railroad's property valid. The Court said:

> "And even though it be granted that the Federal Government utilized the railroad as an instrument in working out its policy toward the Indians, the tax upon the railroad property would be none the less valid."

It is thus plain that the Supreme Court of the United States in its latest utterance has evinced no disposition to recede from the original distinction made in *McCulloch v. Maryland,* between a tax upon the operations of a government agency or its rights to function, and the tax upon the property of such an agency located within the taxing state, and still holds that the latter is not exempt from taxation in the absence of a specific declaraion of Congress to that effect.

This distinction between taxation of the operations or right to function of the governmental agency and taxation of its local property is also clearly recognized in the *Telegraph* cases which were cited by appellees in the trial court as showing that the "means" employed by the Federal Government cannot be taxed by the states.

Williams v. Talladega, 226 U. S. 404; 57 Law Ed. 275, involved a municipal license fee in the nature of an

occupation tax of $100 per year upon the right of the Western Union Telegraph Company to transmit messages. In consideration of permission conferred by Act of Congress to construct and maintain its lines upon the military and post roads of the United States, the company was required as an instrumentality of the Federal Government to transmit messages for the government at reduced rates and give such messages priority over other business.

The license tax did not except from its operation such Federal business. The ordinance was held void as an attempt to tax the right of the company to function as a governmental agency. But the Court, speaking through Justice Day, after reviewing the prior telegraph cases, said:

> "These cases, taken together, establish the proposition that the privilege given under the terms of the act to use the military and post roads of the United States for the poles and wires of the company is to be regarded as permissive in character, and not as creating corporate rights and privileges to carry on the business of telegraphy, which were derived from the laws of the state incorporating the company, and that this permissive grant did not prevent the state from taxing the real or personal property belonging to the company within its borders, or from imposing a license tax upon the right to do a local business within the state."

Western Union Tel. Co. v. Texas, 105 U S., 530; 26 Law Ed., 1067, involved an occupation tax which imposed a specific tax on each message transmitted by the

company. This was in addition to the usual taxes on the real and personal property of the company within the state. The Federal Supreme Court held that in transmitting messages from points within to points without the state the company was an instrument of interstate commerce, and that in transmitting messages for the Federal Government it was a government agency, and that therefore neither interstate messages nor messages for the government could be subjected to the occupation tax. But, referring to the Act of Congress giving to the company the right to use military and post roads, the Court said:

> "The Western Union Company having accepted the restrictions and obligations of this provision by Congress, occupies in Texas the position of an instrument of foreign and interstate commerce, and of government agent for the transmission of messages on public business. Its property in the State is subject to taxation the same as other property, and it may undoubtedly be taxed in a proper way on account of its occupation and business. The precise question now presented is, whether the power to tax its occupation can be exercised by placing a specific tax on each message sent out of the state, or sent by public officers on the business of the United States."

Western Union Tel. Co. v. Attorney General, 125 U. S., 530; 31 Law Ed., 790, likewise sustains our position that an exemption from state taxation of the *property* of a corporation employed as a governmental agency is never implied though such exemption is implied as to its operations or right to function. The Court said:

"While the state could not interfere by any specific statute to prevent a corporation from placing its lines along these post roads, or stop the use of them after they were placed there, nevertheless the company receiving the benefit of the laws of the state for the protection of its property and its rights is liable to be taxed upon its real or personal property as any other person would be. It never could have been intended by the Congress of the United States, in conferring upon a corporation of one state the authority to enter the territory of any other state and erect its poles and lines therein, to establish the proposition that such a company owed obedience to the laws of the state into which it thus entered, and was under no obligation to pay its fair proportion of the taxes necessary for its support."

A clearer recognition of the distinction between taxation of the operations or right to function of a government agency and taxation of its local property, than that made in these telegraph cases can hardly be conceived. They all hold that the operations or right to function of the governmental agency are the means employed by the government, without which the agent cannot serve the government; that state taxation of such operations or rights has a direct and necessary tendency to obstruct or impair the agent's power to serve, hence it is prohibited by necessary implication, but that taxation of the local property of the agency in the same manner as other property in the state, has no such necessary tendency, hence is not impliedly prohibited.

It is no answer to say, as was said by the trial court, that the properties of the Spruce Corporation are "the

only means and instrumentality by which the purpose and employment could be carried out." Obviously the timber lands, mill and railroad of the Spruce Corporation are no more the "means" employed by the government for the production of airplanes, than were the local tracks and rights-of-way of the railroad in the *Thompson* and *Peniston* cases the "means" employed by the government in the transportation of troops, munitions and mails. Obviously the property here taxed was no more the "means" employed for the government's purpose than were the local poles, wires and real estate of the telegraph companies the means employed for the messages in the *Telegraph* cases.

Obviously, equal taxation of the property here involved with other like property in the State has no more direct or necessary tendency to obstruct or destroy the power of the Spruce Corporation to produce timber for airplanes than the tax on the railroad's tracks and rights-of-way, involved in the *Thompson, Peniston* and other railroad cases, had to obstruct or destroy the power of the railroads to carry government troops, war munitions or the mails. It is no more true that this corporation could not produce airplane lumber without its timber lands than it was that the railroads could carry government troops, munitions and mails without their tracks and rights-of-way, or that the telegraph companies could transmit government messages without their poles and wires.

It is too plain for cavil that all these cases hold that the "means" employed by the government are the corporations themselves with their right to be, to operate and to function; that the direct and necessary effect of a state tax on any of these rights would be to obstruct or destroy the power to serve, hence it is impliedly prohibited, but a tax on the local property commensurate with other like property in the state has no such direct or necessary tendency, hence is not impliedly prohibited.

This is the criterion laid down by Chief Justice Marshall in *McCulloch v. Maryland* over a hundred years ago and consistently followed ever since in an unbroken line of decisions. Congress must be presumed to have known of these decisions and that the rule they announced had been followed for a century when it authorized the creation under the State law, and the employment of the Spruce Corporation as a governmental agency. Had it intended or desired to exempt the local property of that corporation from State taxation it must be assumed that in the act authorizing the employment of such agencies it would have so declared. It did not so declare and no implication of such an intention can be reasonably indulged.

In practically every case in which the Federal Supreme Court has held that the "means" employed by the Federal Government are impliedly exempt from state taxation, *the term "means" is defined as the corporate agency itself, its right to operate, to function and to be.*

In none of them is it used as including the local physical property of the agency. In every such case such local property is *expressly excluded* from that term.

The adoption of the Fourteenth Amendment to the Federal Constitution has destroyed the force of the oft-quoted dictum of Chief Justice Marshall in *McCulloch v. Maryland* that "the power to tax involves the power to destroy." The answer is found in the opinion of Judge Field in *County of Santa Clara v. Southern Pacific R. Co.*, 18 Fed., 365, above cited. It is true that in that case the tax on the property of the railroad was held invalid, not on the ground of exemption, but for gross inequality as compared with the taxes on other property in the state, thus impinging the Fourteenth Amendment of the Federal Constitution. The court held that that amendment declaring that no state shall deny to any person within its jurisdiction the "equal protection of the laws" imposes a limitation upon the exercise of all the powers of the state which can touch the individual or his property, including the power of taxation. Judge Field said:

> "Unequal taxation, so far as it can be prevented, is, therefore, with other unequal burdens, prohibited by the amendment. There undoubtedly are, and always will be, more or less inequalities in the operation of all general legislation arising from the different conditions of persons from their means, business, or position in life, against which no foresight can guard. But this is a very different thing, both in purpose and effect, from a carefully devised scheme to produce such inequality; or a scheme, if not so

devised, necessarily producing that result. Absolute equality may not be attainable, but gross and designed departures from it will necessarily bring the legislation authorizing it within the prohibiton. The amendment is aimed against the perpetration of injustice, and the exercise of arbitrary power to that end. The position that unequal taxation is not within the scope of its prohibitory clause would give to it a singular meaning. It is a matter of history that unequal and discriminatory taxation, leveled against special classes, has been the fruitful means of oppressions, and the cause of more commotions and disturbance in society, of insurrections, and revolutions, than any other cause in the world. It would, indeed, as counsel in the *San Mateo case* ironically observed, be a charming spectacle to present to the civilized world, if the amendment were to read, as contended it does in law, 'Nor shall any state deprive any person of his property without due process of law, *except it be in the form of taxation;* nor deny to any person within its jurisdiction the equal protection of the laws, *except it be by taxation.*' No such limitation can thus be ingrafted by implication upon the broad and comprehensive language used. The power of oppression by taxation without due process of law is not thus permitted; nor the power by taxation to deprive any person of the equal protection of the laws."

It is thus made plain that the Fourteenth Amendment constitutes an insuperable bulwark against destruction of a Federal Agency by taxation of its property. By guaranteeing equality of taxation it makes it impossible for any state to destroy such an agency by taxing its property without at the same time destroying every other business enterprise in the state and thus destroying itself.

No such inequality is claimed in the case here. The property of the Spruce Corporation is taxed just as other property in the state is taxed.

It is certainly no more true that "the power to tax involves the power to destroy' a Federal agency, than it is that the power to prohibit state taxation involves the power to destroy the state. This is clearly pointed out in the *Thompson* and *Peniston* cases. In the *Peniston* case the Court said:

> "A very large proportion of the property within the states is employed in execution of the powers of the government. It belongs to government agents, and is not only used, but it is necessary for their agencies. * * * Were they exempt from liability to contribute to the revenue of the states it is manifest that the state governments would be paralyzed. While it is of the utmost importance that all the powers vested by the Constitution of the United States in the General Government should be preserved in full efficiency, and while recent events have called for the most unembarrassed exercise of many of these powers, it has never been decided that state taxation of such property is impliedly prohibited.'

It is the plain purport of these and many other decisions of the Federal Supreme Court that the intention to exercise a power fraught with such potential disaster to these states should never be implied except where the implication is positively essential to the service of the government by its agents. It is equally plain that unless the line of implied exemption from taxation be drawn between taxation of the right of the agent to op-

erate, to function, or to be, and taxation of its local property, where it has been consistently drawn by that Court for a century, there is no line. It is only safe and sane to continue to hold, as has been so long held, that if Congress intends to exempt such property from state taxation it must say so and when it has not so declared, no such exemption shall be implied.

2. *The property of the Spruce Corporation was not owned by nor held in trust for the United States.*

All of this property during the years for which it was taxed stood in the name of the Spruce Corporation by deed absolute, without reservation, condition or defeasance of any kind. The Spruce Corporation actually paid the full consideration therefor from money realized on the sale of its own debenture bonds. That the Spruce Corporation is a separate entity, not endowed with the sovereignty of the United States; that it is not the government nor a part of the government of the United States, but is a private corporation and as such subject to suits both on contracts and tort, are things now conclusively established.

United States v. Strang, 254 U S. 491; 65 L. Ed. 368;

Sloan Shipyards Corp. v. U S. Shipping Board Emp. F. Corp; Astoria Marine Corp.; Fleet Corp. v. Wood, Trustee, 257 U S. ... 66 L. Ed. ....; No. 14 Adv. Op. U. S. Sup. Ct., July 1, 1922, p. 456;

Panama R. Co. v. Minnix, 282 Fed. Rep Adv. Sheets, No. 1, p. 47;
United States v. Matthews, 282 Fed Rep. Adv. Sheets No. 1, p. 266.

The Spruce Corporation is a separate entity, a corporation organized under the laws of the State of Washington. The title of all of this property at the time it was taxed and during the years for which it was taxed was in that corporation. If it was the property of the United States it must be because of some trust created either *expressly* or by operation of law.

It is elementary that the burden of proving a trust in lands contrary to the apparent legal title rests upon him who asserts it. Broadly speaking, there are only three kinds of trusts known to the law. These are (a) express trusts, (b) constructive trusts, and (c) resulting or implied trusts.

3 *Pomeroy, Equity Jurisprudence* (4th Ed.), Sec. 987.

(a) *Express trusts* are "those created by the contract of the parties and intentionally."

Farrell v. Mentzer, 102 Wash., 629-632;
3 *Pomeroy, Equity Jurisprudence* (4th Ed.), Sec. 987.

It is the settled law of the State of Washington that "an express trust cannot be proven by parol testimony." It must be proved by written evidence.

Arnold v. Hall, 72 Wash., 50-52;
Kalinowski v. McNeny, 78 Wash., 681-684;
Croup v. DeMoss, 78 Wash., 128-131-132;
Farrell v. Mentzer, 102 Wash., 629-649-650.

The Federal Courts are of course bound by the construction put upon the laws of the State by the Supreme Court of the State. This is as true in the attempt to assert a trust as in other cases.

Osterman v. Baldwin, 6 Wall., 116; 18 L. Ed., (U. S.) 730.

There is no written evidence in this case even tending to show that the property here in question is or ever was held by the Spruce Corporation in trust for the United States. The deed from the United States to the corporation is a deed absolutely without reservation, condition or defeasance. It does not mention any trust and the corporation is not even referred to as a trustee. There is no other writing declaring any trust. The consideration for the conveyance negatives any trust. The land was actually paid for by the corporation with the proceeds of the sale of debenture bonds of the corporation which were purchased by the United States, and which, so far as they remain unpaid, are still held by the United States.

There are no facts in this case from which any court can find the existence of an *express trust* for any purpose.

(b) *Constructive trusts* are those raised by the doctrines of equity to effectuate justice "where there is no intention of the parties to create such a relation, and in most cases contrary to the intention of the holder of the legal title, and where there is no express or implied written or verbal declaration of the trust." All constructive trusts "may be referred to what equity dominates fraud, either actual or constructive, as an essential element, and as their final source."

3 *Pomeroy, Equity Jurisprudence,* (4th Ed.), Sec. 1044.

Manifestly there is no constructive trust in this case. It is not pretended that the Spruce Corporation acquired title to this property through any fraud or by breach of any duty which it owed to the United States.

(c) *Resulting trusts* are of two types:

First, those arising from gift by will or deed, with an intention *appearing from the face of the instrument* that the legal and beneficial estates are to be separated, but no valid or complete trust being declared *and no consideration stated.*

3 *Pomeroy, Equity Jurisprudence,* (4th Ed.), Secs. 1033-1035.

Second, these trusts arising where the legal estate is conveyed to one person and the purchase price is paid either in whole or an aliquot part thereof by another.

3 *Pomeroy, Equity Jurisprudence,* (4th Ed.), Sec. 1037.

In each of these types "there is always the element, although it is an implied one, of an intention to create a trust." The law raises the trust as a result of this implied intention.

3 *Pomeroy, Equity Jurisprudence,* (4th Ed.), Sec. 1031.

Farrell v. Mentzer, 102 Wash., 620-632-633;

Croup v. DeMoss, 78 Wash., 128-132-133.

There are no facts in this case to sustain a resulting trust of the first type, namely, those arising by implication from the *terms of a gift* by will or deed. The deed in this case is absolute on its face, states a full consideration and contains no mention of a trust or anything from which a trust can be implied. In such a case no extrinsic evidence is ever admissible to raise a trust, in the absence of fraud or mistake.

3 *Pomeroy, Equity Jurisprudence,* (4th Ed.), Sec. 1036.

There are no facts to create a resulting trust of the second type defined by Judge Pomeroy as above noted, namely, that resulting from the payment of the purchase price by one party, the title being taken in the name of another. As in other claims of trust, the burden of proving the trust is upon him who asserts it. Though a resulting trust of this second type may be proven by

parol evidence the proof must be of the strongest character. The rule as to *quantum* of proof is thus stated by the same eminent authority:

> "Where the trust does not appear on the face of the instrument of transfer, a resort to parol evidence is indispensable. It is settled by a complete unanimity of decision that such evidence must be clear, strong, unequivocal, unmistakable, and must establish the fact of the payment by the alleged beneficiary beyond a doubt."
>
> 3 *Pomeroy, Equity Juris.*, (4th Ed.), Sec 1040.

See also

Denny v. Holden, 55 Wash., 22-23;

Croup v. DeMoss, 78 Wash., 128-132-133;

Sewell v. Sewell, 109 Wash., 252-255;

Sheehan v. Sullivan, (Cal.) 58 Pac., 543-544;

Barger v. Barger, (Or.) 47 Pac. 702-704;

Catoe v. Catoe, (S. C.) 10 S. E., 1078-1079;

Hatton v. Cunningham, (Ind.) 62 N. E. 644.

A legion of cases to the same effect might be cited, but these should suffice.

The facts are that the purchase price was paid by the corporation to the United States from the proceeds of the sale of the debenture bonds of the corporation. The facts, so far from establishing a resulting trust in favor of the United States, are conclusive that the Spruce Corporation actually paid the full purchase price and

that the United States by taking the debentures of the corporation which it still holds, became and is a mere creditor of the corporation.

True, the Spruce Corporation is a governmental agency, but that does not make its property the property of the government nor make the corporation a trustee for the government as to such property. True, also, the United States owns all of the stock of the Spruce Corporation, but that does not make the government the owner of the property of the corporation.

Fitzgerald v. Missouri Pac. R. Co., 45 Fed., 313.

In re Greenleaf, (Ill.) 56 N. E., 295.

The decision in the *Sloan case,* holding that the Emergency Fleet Corporation is a separate entity from the United States, conclusively establishes our claim that the Spruce Corporation is a separate entity from the United States. If it is, then property which it holds under deed absolute, without reservation or condition, for which it paid full consideration, is the property of the corporation and not the property of the United States.

There is no *express trust,* since the written evidence contains no declaration of trust. The deed to the corporation is absolute. There is no *constructive trust.* The corporation acquired title to this property through no fraud or breach of duty. There is no *resulting trust.*

The deed recites and the facts show a consideration paid by the corporation.

If there is any trust it must have arisen under some settled principle. Yet these are the only classes of trusts known to the law and the facts here negative every one of them. The courts cannot create some new species of trust in order to defeat a tax any more than for other purposes.

The contracts and operations after the armistice show a purely private use, commencing over two years after the armistice and to continue for ten years thereafter, created by contract of the corporation, enforcable under the laws of this State.

Ownership of capital stock does not carry ownership of corporate property.

Fitzgerald v. Missouri P. S. E. R. Co., 45 Fed. 313;

In re Greenleaf, (Ill.) 56 N. E. 295.

The Gloucester, The Federal Reporter, (Decided Jan. 12, 1923. Advance Sheets Mar. 15, 1923, p. 579.)

In the above case District Judge Morton says:

"When a corporate form of organization has been resorted to for fraudulent purposes, courts under some circumstances disregard it and look to the individuals behind it, but the general rule is that

a corporation is a separate entity distinct from its stockholders.'

It is, of course, true that "courts will not be blinded by form of law," but will look through corporate form to attain justice or prevent fraud, but there is no fraud or injustice in the tax here involved; it is not claimed that it is unequal with other taxes, or that it is excessive in rate, or that it is based upon an excessive valuation, or that it is inherently unjust for any other reason. It is an equal tax upon the property within the State, protected by the laws of the State just as other like property is protected. There is no inherent injustice in this property bearing its equal proportion of the taxes levied for the protection of all property within the State.

That it was never the intention of Congress that the property vested in this corporation should be the property of the United States, is conclusively shown by the act of Congress authorizing the creation of the corporation. That act in terms contemplated that private persons might acquire and own as much as forty-nine per cent of the capital stock of the corporation. Congress was thus plainly of the opinion that the power to select and control the managing directorate of the corporation which would follow from the ownership of a majority of the capital stock as completely as from the ownership of all, was an ample guaranty that this property would be used by the corporation for the desired purpose of producing airplane timber, without any declaration of any

trust for or retention of any owneship by the United States in the property itself.

Suppose that private persons had acquired (as they might have done under the Act of Congress) 49 per cent, or any other part, of the capital stock of the corporation. Would anyone then have claimed that the property of the corporation was the property of the United States held in trust for the United States, either in whole or in part? Would anyone then have claimed that a part of this property, proportioned to the capital stock held by the United States, exempt from State taxation, and that the balance was not? We apprehend that no one would have seriously advanced either of these views.

Again, as we have pointed out, the very manner in which the operations of this corporation were financed, is conclusive evidence that the ownership of the property was not intended to be retained by the United States nor held in trust for the United States. It was financed and the very property here in question was purchased with the proceeds of the sale to the government of bonds of the corporation, which, so far as they have not been paid, are still held by the government.

These things are not mere matters of corporate form but are matters of substance going to show the intention of Congress in enacting the law authorizing the formation of this corporation under the laws of the State of Washington.

Let us examine a few of the provisions of that act:

By Section 1 it is left to the director of aircraft to choose the state under the laws of which the corporation was to be formed and no restriction is placed upon his powers in that regard except the total investment shall not exceed $100,000,000.

By Section 2 that officer is given permission to subscribe on behalf of the United States for the capital stock of the corporation and no restriction is placed upon the nature or extent of the liability so assumed. In the same section he is authorized to buy such evidences of indebtedness as the corporation may offer for sale. He may sell the interest of the United States in the corporation, either all or in part, the only restriction being that the United States shall not be made a minority stockholder.

By Section 3 it is provided that one year after the signingof peace the Director of Aircraft shall, "on behalf of the United States as a stockholder," institute proceedings in the proper State Court to dissolve the corporation and upon such dissolution the corporation "shall be liquidated and the assets distributed in accordance with the laws" of the State. This provision is without any restriction.

These provisions make it too plain for doubt that the United States assumed the status of, and intended to exercise, and can only exercise in this corporation, the powers and rights of a *stockholder*. If the Federal

Government had intended to exercise the sovereign governmental control over this corporation which it exercises over its boards and departments, why the provision that it should always retain a controlling interest in the voting power of the corporation? If the Government had intended to retain the ownership of the property vested in this corporation, why the provision that on its dissolution the assets be distributed by the Court of the State in accordance with the laws of the State? If it ever intended that this corporation should hold its properties merely in trust for the Government, why the *inconsistent* provision that private persons might acquire and own as much as forty-nine per cent of the capital stock?

Section 4 of the Act, touching the personnel of the officers of the corporation, expressly provides that the corporation may employ "civilians in the manner customary in the conduct of ordinary business under corporate organization." This further manifests a plain intent that this corporation shall operate as a mere private corporation under the laws of the State.

Section 5 expressly authorizes the Director of Aircraft to transfer to the corporation any interest of the United States in any contracts necessary for carrying out the corporate business and that he may transfer by appropriate instrument "the title to any lands plants, railroads or equipment used in or in connection with the production of aircraft, aircraft equipment or materials therefor."

If it had been intended that the Government should retain the ownership of such contracts and property and that the corporation should take and hold them as a mere trustee, what easier or more natural than to say so in the act authorizing the transfer? These properties were actually transferred to the corporation by deed absolute, without reservation, condition or declaration of any trust, an instrument of that officer's own selection. Thus in carrying out the legislation which the War Department had doubtless inspired and intrusted to its Director of Aircraft for carrying out, he construed it as contemplating no reservation of ownership in, or trust for, the United States. Such a contemporaneous construction by the officer intrusted by the statute itself with the carrying out of its own provisions is entitled to the greatest weight and will be followed by the courts unless there are the most cogent reasons to the contrary.

United States v. Moore, 95 U. S., 760; 24 L. Ed., 588;

Brown v. United States, 113 U. S., 568; 28 L. Ed., 1079;

Eells v. Ross, (9th Circuit) 64 Fed., 417-420;

Jacobs v. Prichard, 223 U. S., 200-214; 56 L. Ed., 405-409.

The case of *King County, Washington, v. The U. S. Shipping Board Emergency Fleet Corporation,* decided by the Ninth Circuit on September 5, 1922, will no doubt

be cited by opposing counsel. There are certain considerations which vitally distinguish that case from this.

In the first place, the property there in question was not acquired by the Fleet Corporation with funds coming from the sale of its own bonds or debentures, nor even, as the Court in substance says, from the sale of its capital stock. It was purchased with money directly appropriated by the government for that purpose, the naked title being taken in the name of the Fleet Corporation. This is apparently the controlling factor in that decision. Whereas in this case the property was purchased from the United States by the Spruce Corporation and the government actually took in payment therefor the debenture bonds of the Spruce Corporation in the full value of the property, which bonds, so far as they have not been paid by the corporation, are still held by the government. The government thus became a mere creditor of the corporation, not the owner of the corporate property.

In the second place, the Fleet Corporation was organized under the laws of the District of Columbia, which were enacted by Congress itself. Whereas the Spruce Corporation was organized under the laws of the State of Washington. It may be, as said in the *King County case,* that it is one thing for the government to commit to its agent the control of public property and authorize it to contract and to sue and be sued in relation thereto, "but quite another thing to permit such property to be encumbered with burdens in the imposition of which

neither it nor its agent has any part." That language may have persuasive force as applied to the Fleet Corporation, but hardly as applied to the Spruce Corporation. The government, by organization of the Spruce Corporation under the laws of the State of Washington, did have just that part in imposing upon the local property of the corporation the same burdens which the laws of that state place upon other like corporate property. By causing the Spruce Corporation to be organized under the laws of the state it made that corporation a creation of the state deriving its franchise and its right to be from the state law and as a corallary subjected its property to the same burdens of taxation as other like corporate property in the state. As said in the case of *Thompson v. Union Pac. R. Co., supra*:

> "But we are not aware of any case in which the real estate, or other property of a corporation not organized under act of Congress, has been held to be exempt, in the absence of express legislation to that effect, to just contribution, in common with other property, to the general expenditure for the common benefit, because of the employment of the corporation in the service of the government."

Further in the same case it is said:

> "We do not think ourselves warranted, therefore, in extending the exemption established by the case of *McCulloch v. Maryland,* beyond its terms. We cannot apply it to the case of a corporation deriving its existence from state law, exercising its franchise under state law, and holding its property within state jurisdiction and under state protection."

As said in *County of Santa Clara v. So. Pac R. Co., supra,* after citing the *Thompson case*:

> "But we are of the opinion, yielding to the decision cited, that when the instrumentality is the creation of the state—a corporation formed under its laws—and is employed or adopted by the general government for its convenience, although to enlarge its use and render it more available, additional privileges and benefits are conferred by the government upon the corporation, it remains subject to the taxing power of the state, unless Congress declares it to be exempt from such power."

See also to same effect:

Western Union Tel. Co. v. Attorney Gen., 125 U. S., 530; 31 Law Ed., 790;

Williams v. Talladega, 226 U. S., 404; 57 L. Ed., 275.

Congress, when it passed the act authorizing the organization of corporations under state laws, must be presumed to have known of these decisions of the Federal Supreme Court. If it had intended that such corporation should be wholly exempt from state taxation it would have so declared.

In the third place, the provisions of Section 4 of the Act of June 5, 1920, touching the Fleet Corporation, which the Circuit Court in the *King County case* construed as giving to the government an "unqualified right to dispose of property, without any action on the part of the corporation, and to transfer it to the Shipping

Board," has no counterpart so far as can be found in the legislation touching the Spruce Corporation. There is nothing in the legislation touching the Spruce Corporation evidencing an intention on the part of the government to retain any control over the property vested in that corporation other than what it might exercise as a majority stockholder. Even on a dissolution of the corporation any residue of the property remaining undisposed of by the corporation can pass to the United States only as a stockholder by order of the State court in a proceeding instituted pursuant to state law. This is specifically provided in Section 3 of the Act.

We submit that, insofar as the decision in the case of *King County, Wash., v. U. S. Shipping Board E F. Corp.* is based upon the theory that the states are without power to levy any tax upon the property of a corporation employed as a governmental agency without permissive legislation of Congress so to do, *it is directly contrary to a line of decisions of the Federal Supreme Court extending back for a century,* including the *McCullach case,* the *Thompson case,* the *Peniston case,* the *Telegraph cases* and many other cases which we have cited and quoted elsewhere in this brief.

It is said in the *Thompson case,* 9 Wall., 579-592; 19 Law Ed., 792-798:

> "No one questions that the power to tax all property, business and persons, within their respective limits, is original in the state and has never been surrendered. It cannot be so used,, indeed, as to defeat

or hinder the operations of the National Government; but it will be safe to conclude, in general, in reference to persons and state corporations employed in government service, that when Congress has not interposed to protect their property from state taxation, such taxation is not obnoxious to that objection."

It is said in the *Peniston case,* 18 Wall., 5.50; 21 Law Ed., 787-791:

"That the taxing power of the state is one of its attributes of sovereignty; that it exists independently of the Constitution of the United States, and underived from that instrument; and that it may be exercised to an unlimited extent upon all property, trades, business and avocations existing or carried on within the territorial boundaries of the State, except so far as it has been surrendered to the Federal Government, either expressly or by necessary implication, are propositions that have often been asserted by this court. And in thus acknowledging the extent of the power to tax belonging to the States. we have declared that it is indispensable to their continued existence. No one ever doubted that before the adoption of the Constitution of the United States, each of the States possessed unlimited power to tax, either directly or indirectly, all persons and property within their jurisdiction, alike by taxes on polls, or duties on internal production, manufacture or use, except so far as such taxation was inconsistent with certain treaties which had been made. And the Constitution contains no express restriction of this power other than a prohibition to lay any duty of tonnage, or any impost, or duty on imports or exports, except that may be absolutely necessary for executing the State's inspection laws."

The decision in the *King County case* quotes from the opinion in *Owensboro National Bank v. Owensboro,* 173 U. S., 664-668; 43 L. Ed., 850, as follows:

> "It follows then necessarily from these conclusions, that the respective states would be wholly without power to levy any tax, direct or indirect, upon national banks, their property, assets or franchises, were it not for the permissive legislation of Congress."

That this language, if given the meaning accorded to it in the *King County case,* expresses the direct converse of the rule as expressed in the above quotations from the *Thompson* and *Peniston* cases, is self-evident. That the true rule is that expressed in those cases is also self-evident when it is remembered that the powers of the states are *original* powers and the powers of the Federal Government are *granted* powers.

Moreover, the above language quoted from the *Owensboro case* was used in relation to national banks and the governing statute (U. S. Rev. Stat., Sec. 5219) expressly says:

> "Nothing herein shall be construed to exempt the real property of associations from either state, county, or municipal taxes, to the same extent, according to its value, as other real property is taxed."

This language of the statute is in no sense a permission to tax. Plainly no such permission was necessary. On the contrary, it was a mere disclaimer on the part of Congress of any intention to *prohibit* state taxation of

real estate belonging to national banks, which is a very different thing. If express permission were necessary, why any necessity to disclaim an intention to prohibit? The statute thus clearly defining its own meaning it is manifest that if the above quoted language from the *Owensboro case* was intended to apply to real estate it was wholly unnecessary to the decision and hence *obiter dictum*. If, however, it was intended to apply only to the *franchises* of national banks, (and we think a reading of the opinion will show it was so intended) then it is sound, since the exemption of the corporate *franchises*, the right to function and to be, of a governmental agency is necessarily implied as an incident to the granted powers of the Federal Government.

On what principle can it be asserted that a sovereign state is without power, and especially when unprohibited by national legislation if it could be so prohibited, to maintain itself by taxing the property within the state belonging to a citizen of the state?

On what principle can property of a citizen protected by state sovereignty and subjected to state processes, purchased and held under state law, be exempt from burden, with other property, of maintaining such sovereignty to which it owes its existence?

Congress when it authorized an application to be made to the sovereign state for permission to create under state laws a citizen of such state, did not attempt to exempt such citizen or its property from the duty of con-

tributing to the support and existence of the state creating such citizen corporation. This was no doubt deliberate for at the time such national legislation was enacted no one could hazard a guess as to the extent to which this Government would have to go to win the war. It was possible and even probable that almost every field of activity would be called for war service, and if the properties to be used in such activities were to be exempt from state taxation, the states' ability to function would be necessarily much impaired, if not destroyed, and its citizens impoverished if property used in war activities were exempt and remaining property had to carry the entire burden.

On what principle can one state corporation be distinguished from another? Does the personnel of ownership of stock differentiate one from another so that a state corporation whose stock is owned by individual owners must pay the state taxes upon its property, whereas if the stock was owned by the United States it would not? Such corporations may be engaged exclusively in serving the government either by reason of contractual relation or by reason of the fact that the government has purchased or subscribed for a major part of the stock and hence enabled to dominate the activities of the corporation.

This state corporation exists solely under and by reason of state law; it is obedient and must conform to all laws of the State of Washington.

The State of Washington incorporation laws do not say that a corporation formed under and existing by reason of its laws is subject to all state laws *except the tax laws.* This corporation had to file articles with the state officials and if such articles had contained such an exemption they would not have been accepted.

If it was intended to raise a trust for or reserve title in the United States in the properties of this state corporation, there would have been some such suggestion in the deed of conveyance or in the national legislation.

The Constitution of the State of Washington, Article XII, Section 6, provides:

"Corporations shall not issue stock, except to *bona fide* subscribers therefor, or their assignees; nor shall any corporation issue any bond or other obligation for the payment of money, except for money or property received or labor done."

And Article VII, Section 1, provides:

"All property in the state not exempt under the laws of the United States or under this constitution, shall be taxed in proportion to its value, to be ascertained as provided by law. The legislature shall provide by law for an annual tax sufficient, with other sources of revenue, to defray the estimated ordinary expenses of the state for each fiscal year."

Section 2 provides:

"The legislature shall provide by law a uniform and equal rate of assessment and taxation on all

property in the state, according to its value in money, and shall prescribe such regulations by general law as shall secure a just valuation for taxation of all property, so that every person and corporation shall pay a tax in proportion to the value of his, her, or its property."

Section 3 provides:

"The legislature shall provide by general law for assessing and levying of taxes on all corporation property as near as may be by the same methods as are provided for the assessing and levying of taxes on individual property."

Under such provisions a claim that the Spruce Corporation was only a matter of form; that the issuance of stock and bonds a matter of book-keeping would be to claim that a fraud was intended and practiced upon the State of Washington.

The fact that the United States owns the stock would not change the principle that must apply if the United Sates only owned fifty-one per cent as it was authorized by the Acts of Congress. It would not make it the owner of the property of the corporation any more in the one case than in the other.

There must an an underlying principle of general application. The United States cannot be singled out from other owners of stock. It cannot be asserted that when it owns the stock it owns the property unless the

same may be asserted of all owners of stock in state corporations.

If the United States as a stockholder owns the property, then the corporation is a fraud on the Constitution of the State of Washington; a mere shell surrounding nothing, with no independent existence.

Such a principle must further be applicable to a state corporation already formed under state law, 51 per cent of whose stock the United States has bought. In such case would the purchase by the United States of stock and bonds change the ownership of the property from the corporation to the purchaser or convert the corporation into a trustee?

On what principle can it be asserted that the national sovereignty can, by implication (or by express enactment which is not the case here) destroy the state sovereignty? The states must exist to maintain the "indissoluble union of the indestructible states."

When the Spruce Corporation applies to the State of Washington for a charter, it necessarily subjected its property to the just burdens, with other citizens, of state taxation to support the sovereignty to which it owned is existence and allegiance. It assumed all the burdens of citizenship and obedience to the laws of the state upon which it depended for existence and protection.

We respectfully submit that *Question I* should be answered in the negative and *Question II* in the affirmative.

Respectfully submitted,

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OCTOBER TERM, 1923.

CLALLAM COUNTY, WASHINGTON; William A. Nelson, Sheriff of Clallam County, Washington; E. C. Stewart, Treasurer of Clallam County, Washington, et al.,

v.

THE UNITED STATES OF AMERICA AND the United States Spruce Production Corporation.

No 255.

ON CERTIFICATE FROM THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT.

BRIEF FOR THE UNITED STATES.

STATEMENT.

This case comes before this Court upon a certificate from the Circuit Court of Appeals for the Ninth Circuit, presenting two questions:

I. Did the United States District Court have jurisdiction of the suit?

II. Is the property of the Spruce Production Corporation subject to State taxation? (Rec. p. 6.)

The gradual evolution of the activities of the Government in the production of aeroplane material during the war may be traced in the following statutes:

June 3, 1916, 39 Stat. p. 213, c. 134, Sec. 120.
May 12, 1917, 40 Stat. p. 42, c. 12.
June 15, 1917, 40 Stat. p. 187, c. 29.
July 24, 1917, 40 Stat. p. 245, c. 40, Sec. 9.
Oct. 1, 1917, 40 Stat. p. 296, c. 61.
Oct. 6, 1917, 40 Stat. p. 356, c. 79.
May 20, 1918, 40 Stat. p. 556, c. 78.
July 9, 1918, 40 Stat. p. 849, c. 143.
July 9, 1918, 40 Stat. p. 888.

The creation of the United States Spruce Production Corporation, and the employment by it of both military and civilian forces, was one of the final steps in this series of efforts.

In May, 1918, the President, by virtue of the power conferred upon him by the so-called Overman Act (Act of May 20, 1918, c. 78, 40 Stat. 556), created the Bureau of Aircraft Production and a Division of Military Aeronautics, the executive officer of which was the Director of Aircraft Production.

The Act of July 9, 1918, 40 Stat. c. 143, p. 888, provided (Sec. 1): That the Director of Aircraft Production might form, under the laws of the District of Columbia or those of any State, corporations for the production of aircraft, equipment, and materials and for the building and operation of railroads in connection therewith; (Sec. 2) That he might, on behalf of the United States purchase not

less than a majority of the voting stock and all or part of the nonvoting stock, bonds, notes, debentures, or other securities, and with the approval of the Secretary of War might sell the same. provided that the United States should never become a minority holder of voting stock therein; (Sec. 3) That, within one year after the signing of a treaty of peace he should institute proceedings for dissolution; (Sec. 4) That the Secretary of War might assign enlisted men or commissioned officers to carry on the work of such corporations; (Sec. 5) And that the Secretary of War, acting through the Director of Aircraft Production, might transfer to such corporations "any interest of the United States in any existing contracts for aircraft, aircraft equipment, or materials therefor, and the title to any lands, plants, railroads, or equipment used in or in connection with the production of aircraft, aircraft equipment, or materials therefor, on such terms as the Secretary of War, acting through the Director of Aircraft Production shall deem fit."

It was in pursuance to the authority given in this Act that the Director of Aircraft Production, on August 21, 1918, caused the United States Spruce Production Corporation to be incorporated under the laws of the State of Washington. The United States at all times owned all of the capital stock issued, and all of the certificates therefor stood in its name save the shares necessary to qualify the directors. These were issued in the names of the directors who executed assignments to the Secretary of War, endorsed

the certificates in blank and deposited them with the secretary of the corporation (Rec. pp. 2, 3). The United States purchased all of the bonds (Rec. p. 4).

On January 29, 1919, subsequent to the Armistice, the Bureau of Aircraft Production and the Division of Military Aeronautics were consolidated, forming the Air Service, as then provided for by Army regulations, which functioned under the Director of Air Service. This title was later changed to Chief of Air Service. The Air Service, with its powers and duties as provided for by Army regulations, continued until June 4, 1920, on which date the National Defense Act, as amended, became effective. This Act provided for the office of Chief of Air Service. (41 Stat. c. 227 p. 768.)

Army Regulation No. 95–5, November 17, 1921, Paragraph E, as prescribed by the Chief of Air Service, is as follows:

> I will, in accordance with instructions from the Secretary of War, exercise administrative supervision over the liquidation of the Bureau of Aircraft Production and the United States Spruce Production Corporation.

Other relevant facts concerning the creation and activities of the Spruce Production Corporation are contained in the certificate from the Circuit Court of Appeals. (Rec. pp. 2–6.)

ARGUMENT.

I.

First Certified Question.

Did the United States district court have jurisdiction of the suit?

The jurisdiction of the United States District Court to entertain this suit rests upon two grounds: (A) That the suit has been brought by the United States, and (B) That it arises under the Constitution of the United States.

A.

The suit has been brought by the United States.

The United States has instituted this suit, not merely for the purpose of giving a Federal court jurisdiction, but to assert its right as a sovereign and to claim for its property and for one of its legally constituted agencies immunity from taxation by a State. It is a proper, if not necessary, party plaintiff, (*a*) because of its pecuniary interest (*Dugan* v. *United States*, 3 Wheat. 172, 180; *Cotton* v. *United States*, 11 How. 228, 231), and (*b*) because of its public duty to keep and maintain its property and the exercise of its sovereign powers free and untrammeled. (*In re Debs*,, 158 U. S. 564, 584; *United States* v *Rickert*, 188 U. S. 432, 444.)

The rule that a stockholder's remedy is through an action by the corporation, if it be willing to sue, has no application to the case at bar, for the reasons upon which it is founded do not exist under the circumstances of this case. *Cessante ratione legis cessat et ipsa lex.*

B.

The suit arises under the Constitution of the United States.

This suit must be finally determined upon the merits by deciding whether the limitation upon the taxing power of a State, which is implied in the constitutional provision that "This Constitution, and the laws of the United States which shall be made in pursuance thereof * * * shall be the supreme law of the land" (Constitution, Article VI, Clause 2), shall be so construed as to relieve from State taxation the property of the United States Spruce Production Corporation. Clearly it is a case arising under the Constitution. A Federal question is involved whenever it appears that some right, privilege, or immunity on which recovery depends, will be defeated by one construction of the Constitution or sustained by the opposite construction. (*Starin* v. *New York*, 115 U. S. 248, 257; *Cohens* v. *Virginia*, 6 Wheat. 264, 379; *Jetton v. University of the South*, 208 U. S. 489.)

II.

Second Certified Question.

Is the property of the United States Spruce Production Corporation subject to State taxation?

For more than a century since the decision by this Court of the celebrated case of *McCulloch* v. *Maryland*, 4 Wheat. 316 (1819), it has been conceded that "the States have no power, by taxation or otherwise, to retard, impede, burden, or in any

manner control the operation of the constitutional laws enacted by Congress to carry into execution the powers vested in the Federal Government." No tax imposed by any State can be sustained if its effect be to impose a burden, howsoever light, upon the activities or operations of the United States.

Inasmuch as the determination of the issue now before the Court will depend upon the proper application of the fundamental principles laid down in that case, it may be pardonable to note precisely what was involved and what was decided in that case.

McCulloch v. *Maryland*, 4 Wheat. 316 (1819) involved a statute of Maryland which provided that it should not be lawful for any bank engaged in business within the State but not incorporated under its laws to issue notes excepting in certain denominations and upon stamped paper to be purchased from the State, unless such bank should pay annually, in advance, for the use of the State, the sum of $15,000. Penalties for failure to comply with the provisions of this act were sought to be recovered from the Second Bank of the United States, a corporation which was organized under an act of Congress to do a general banking business, and had established a branch at Baltimore.

Two questions were involved—(1) whether the incorporation of the bank was within the powers vested by the Constitution in the Federal Government, and (2) whether the State law was valid.

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The first of these questions is not of interest here, for it is conceded that the provisions of the Act of Congress, in pursuance of which the United States Spruce Production Corporation was incorporated as a means for prosecuting a great war, were clearly within the powers of the Federal Government. Upon the second question, which is material to the present inquiry, this Court held that the statute of Maryland was not valid.

The distinguished Chief Justice who delivered the opinion found no express provision in the Constitution granting to the Bank immunity from State taxation, nor any express limitation upon the taxing power of the State which checked its hand. On the contrary, he recognized the taxing power as one of the incidents of sovereignty, which the States had in nowise surrendered upon the formation of the Union. The decision rested upon the implied limitation of the scope of the State's taxing power, which arose out of the relations created by the Constitution between the United States and the several States. "This Constitution and the laws of the United States which shall be made in pursuance thereof * * * shall be the supreme law of the land." The Constitution and the laws of the United States can not be supreme unless their operation be absolutely free from and unfettered by the enactments of any State.

From this basic proposition four conclusions followed. These Chief Justice Marshall himself stated in a later case, *Weston* v. *City Council of Charleston*, 2 Pet., 449, 467, in the following words:

(1) That all subjects over which the sovereign power of a State extends are objects of taxation; but those over which it does not extend are, upon the soundest principles, exempt from taxation.

(2) That the sovereignty of a State extends to everything which exists by its own authority or is introduced by its permission; but not to those means which are employed by Congress to carry into execution powers conferred on that body by the people of the United States.

(3) That the attempt to use the power of taxation on the means employed by the Government of the Union in pursuance of the Constitution, is itself an abuse, because it is the usurpation of a power which the people of a single State can not give.

(4) That the States have no power, by taxation, or otherwise, to retard, impede, burden, or in any manner control the operation of the constitutional laws enacted by Congress to carry into execution the powers vested in the General Government.

Applying these principles to the case then before it this Court held that, as the Bank was a means or instrumentality employed by the United States to carry out its constitutional powers, a regulation and tax, such as Maryland had imposed upon its operations was unconstitutional and void.

The obvious and imperative necessity for complete freedom of the sovereign powers of the United States from control or interference by any State, stands out clear as the basis of decision of this great

constitutional landmark. A half century later, in *Railroad* v. *Peniston*, 18 Wall., 5 (1873), it is again declared by Mr. Justice Strong (p. 36):

> It is, therefore, manifest that exemption of Federal agencies from State taxation is dependent, not upon the nature of the agents or upon the mode of their constitution, or upon the fact that they are agents, but *upon the effect of the tax;* that is, upon the question whether the tax does in truth deprive them of power to serve the government as they were intended to serve it, or does hinder the efficient exercise of their power. (Italics ours.)

This is the criterion by which must be determined the validity of any State tax which is questioned on this ground.

The principle of "noninterference" announced in *McCulloch* v. *Maryland*, *supra*, may be applied to Federal agencies or instrumentalities of many different kinds. Among the cases which have called for the application of the principle by this Court, the instant case is unique.

In one of the cases, which involved the right of a State to tax the property of a railroad company, Mr. Justice Chase said (*Thomson* v. *Pacific Railroad* 9 Wall., 579, 591):

> But we think there is a clear distinction between the means employed by the government and the property of the agents employed by the government. Taxation of the agency is taxation of the means; taxation of the property of the agent is not always, or generally, taxation of the means.

From this language the Appellants have drawn the conclusion that State taxation of the right of a Federal agency *to be, to operate,* and *to function,* is impliedly forbidden by the Constitution; but that taxation of the *property* of such agent is *never* so forbidden. (Brief for Appellants, pp. 27, 29, 33, 37, 40, and 42.) It is to be noted that this is precisely what Mr. Justice Chase carefully avoided saying. They vary the language of the last line quoted, from "taxation of the property of the agency is *not always* or *generally* taxation of the means," to "taxation of the property of the agency is *never* taxation of the means." The Court clearly recognized that in some cases taxation of the property of the agency may amount to *taxation of the means.* It is not *always* so. Nor is it *generally* so. However, agencies such as the Spruce Production Corporation are unusual, and bear an unusual relation to the Federal Government; and the Court clearly recognized the possibility of the creation of such an agency.

We are quite willing to concede that in all the cases cited in the Appellant's brief, save one (*Owensboro National Bank* v. *Owensboro,* 173 U. S. 664), this Court has said that taxation of the property of the agencies or instrumentalities there involved did not amount to an interference with the operations, functions, and activities of the Federal Government. But we can not admit that taxation of the property of the Spruce Production Corporation is not such an interference.

We believe the property of the United States Spruce Production Corporation is exempt from State taxation for two reasons:

A. The Corporation is of such character that taxation of its property is in fact taxation of a means or instrumentality of the Federal Government and imposes a burden upon the United States.

B. The property of the corporation is in fact the property of the United States.

A.

The United States Spruce Production Corporation is of such a character that taxation of its property is in fact taxation of a means or instrumentality of the Federal Government and imposes a burden upon the United States.

The Government of the United States in the exercise of the extensive powers vested in it, acts in a variety of ways and employs means, agencies, and instrumentalities of varying character.

It has officers, boards, and commissions whose relations with, and responsibilities to, it are most intimate and direct. Their activities are the activities of the Government and any restraint upon or regulation of them is a direct interference with the exercise of Federal powers. It is held that a State is without power to impose a tax upon their occupations or upon the emoluments of their offices because in agencies of this character such tax would impose a burden upon their ability to serve the Federal Government. As to property, real or personal, that which belongs to them personally is clearly subject to the taxing power of the State; but that which is com-

mitted to their custody or control by the United States and which is used in the performance of services to it is exempt from taxation. To tax it would impose a burden upon the Federal Government.

The United States, in the exercise of its powers, may create corporations. In such cases the granting of the corporate franchise is a Federal power. The United States is vitally interested in the right or franchise of these bodies to be corporations and to exercise their charter powers. A tax upon their franchise or their right to do business would be an interference with the power to create them. For, as Chief Justice Marshall said, "The power to destroy (to tax) may defeat and render useless the power to create." Regardless of whether such corporations, when formed, perform any services for the Government or not, it is interested in their existence and operation in the economic and industrial life of the people. A State can not tax their franchises or operations. Beyond this, however, the Federal Government is not bound, nor does it desire to exercise its power to give any undue preference to them. They engage in private or quasi-public business and they take their chance of survival with the individuals and corporations operating under franchises granted by the several States. They must bear the taxes upon their property in common with other business entities. The mere fact that they hold a Federal franchise does not exempt their property from taxation, for taxation of their property does not infringe upon the exercise of any Federal power.

The United States, in the exercise of its powers, may also grant franchises to corporations which have been created by the several States. These Federal franchises are exempt from taxation for the same reasons which we have already observed. The Federal power to grant them may not be interfered with by a State. Property of these corporations, however, is subject to taxation. That does not retard or impede any Federal function.

The United States may also enter into contracts with corporations created by it or by the States for the transaction by them of some Government business—to transport the mails, to haul Government property, to transmit and deliver Government messages, or to furnish to the Government material or supplies. It matters not whether such contracts were entered into at the time of their incorporation or afterwards, or whether the consideration given by the Government was a grant of land, the grant of a franchise, or a money payment. The relation with the Government is purely contractual and the immunity of such corporation from State taxation goes only so far as is necessary to keep such contract free and clear of any encumbrance or interference by the State. The actual business transacted under such contracts is Government business and the States can not by taxation or otherwise interfere with it. But the exemption does not extend to the business which the corporation transacts in its private capacity nor to the property which it employs.

When the United States thus enters into a contract with an independent contractor which is engaged in an independent business for its own profit, the Government exercises no supervision or control over it other than that stipulated in the contract. The United States is concerned only with the execution of the contract, a thing which the contractor has engaged to perform, notwithstanding its liability to State taxes or any other burdens or demands upon it. With the property of such contractor the Government is not concerned nor is any tax upon such property a burden upon it or an interference with the exercise of its powers.

Immunity from State taxation, in all of these cases, extends so far, and only so far, as is necessary to preserve the exercise of Federal powers free from control or encumbrance by the State; and the exemption of Federal agencies does not depend "upon the mode of their constitution * * * but upon the effect of the tax." (*Railroad Company* v. *Peniston*, 18 Wall. 5, 36.)

In the land-grant-railroad and the post-road-telegraph cases, relied upon by the Appellants, the agencies involved were of the kind which we have just described. The claim for immunity in each case was based upon one or both of two grounds—either that the corporation held a Federal franchise or that it had a contract under which it was doing some business for the Government. In each case it was held that the Federal franchise and business

could not be taxed, but, as each of these corporations was extensively engaged in private business, it was quite properly held that their property was not exempt. Those decisions are authority for the proposition, that in the case of agencies which are primarily private enterprises holding Federal franchises or having contractual relations with the United States, the taxation of their property is not a burden upon the exercise of the powers of the Federal Government. They do not hold that State taxation of the property of agencies such as the Spruce Production Corporation is valid.

The problem in any given case can not be solved merely by determining in the first instance whether the agency in question has a connection with the Federal Government, and then applying, with Procrustean rigidity, the rule that its functions are exempt from, and its property is subject to, taxation by a State. In each case, regard must be had to the Federal authority under which the agency is created or is functioning, to the nature of the agency and its relations to the Government, to its purposes and the character of its operations, and to the origin, nature, and use of its property. It is only from a consideration of all these matters that it can be determined whether the taxation of the property of the agency imposes a burden upon, or interferes with the free use of, powers of the Federal Government.

The United States Spruce Production Corporation was created in pursuance to the provisions of the

Act of Congress of July 9, 1918, 40 Stat. 888, c. 143, by four civilians and three Army officers, who, at the instance of the Director of Aircraft Production of the United States, prepared, executed, and acknowledged the articles of incorporation. (Rec. p. 2.) In so doing these incorporators were not acting as individuals, but were agents of the United States. They conformed to the laws of the State of Washington, obtained a charter from that State, and in the technical sense the corporation is a corporation of the State of Washington. But to say that it is a corporation of the same character as any other private corporation formed under the laws of Washington and having contractual relations with the Federal Government, is to lose sight entirely of its genesis and *raison d'être*. A corporation bearing the same relation to the United States as this corporation could not come into being without the enabling legislation of Congress.

As to its powers and the scope of its activities, they were limited—not by the laws of Washington, but by the Federal laws—to the production of aircraft materials and such operations as were incident thereto. Its purpose was to serve the needs of the Nation in a great war, and not to exercise in the field of private industry and commerce the charter powers which the State of Washington gave it. Its "activities were wholly directed to the Government's program of production of aeroplane lumber." (Rec. p. 3.)

As to its property, it was all acquired by funds derived from the United States. (Rec. p. 6.) Some of the property belonged to the United States before the corporation was formed. This was transferred to it for $274,164.76 and the assumption of outstanding obligations of the United States incurred in connection with the property. (Rec. p. 3.) Every dollar subscribed and paid in upon the stock was paid by the United States, and all bonds sold by the corporation were sold to the United States. (Rec. pp. 3–4.) In fact the character of the company was such and the provisions of its bonds were such that neither stock nor bonds could have been sold in the investment market. The payments made by the United States for stock and bonds and the payment of $274,164.76 by the corporation were merely methods of bookkeeping.

The life of the corporation was limited by Act of Congress (July 9, 1918, 40 Stat. 889, c. 143, Sec. 3) to the duration of the war and such time thereafter as might be necessary for the purpose of liquidation. The corporation is engaged to-day solely in liquidation. (Rec. p. 4.)

These facts make it clear that this corporation is not within any of the classes which have heretofore been dealt with by this Court in the cases cited by the Appellants.

It was not incorporated by the Act of Congress as a national bank, nor did it hold a franchise from the Federal Government as the railroad and telegraph companies referred to; but it was incorporated in

pursuance to Federal laws, exclusively to serve the national needs; its purposes and activities were limited by the Government; its operations entirely controlled by the United States; its life determined by the duration of the national emergency; it was subsidized, supported, and maintained by the United States and all profits and losses resulting from its operations inured to or were borne by the United States. It seems idle to say that a tax upon the property of such a corporation is not a tax upon the activities of the United States or a burden upon the exercise of its constitutional powers.

By whom would such a tax be paid? By the corporation in the first instance, but out of moneys provided by the United States. And the effect of such tax would be either to reduce by the amount of the tax the effective scope of the activities of the corporation, or to call upon the Treasury of the United States to make payment. It could not pay the tax out of its earnings in the conduct of a private business, for it conducted none; nor could it pay out of the sale of capital assets unless it converted to that purpose property already dedicated to the purposes of the Federal Government.

If such a corporation be compelled to retrench, what activities will be curtailed or what business be suspended? Obviously, the activities and the business of the United States.

In the case of such a corporation, taxation of its property is taxation of a means, agency, or instrumentality of the Federal Government, and does

impede the free exercise of Federal powers. The distinction is between a corporation which is *exclusively* and one which is *incidentally* an agency of the Government.

In *Owensboro National Bank* v. *Owensboro*, 173 U. S. 664, it was held that a State tax upon the intangible property of a national bank was not valid. This decision, following *Thomson* v. *Pacific Railroad*, 9 Wall. 579, and *Railroad Company* v. *Peniston*, 18 Wall. 5, recognizes a difference between national banks, which are in themselves governmental instrumentalities, and railroads which are primarily private enterprises performing *inter alia* Federal services (*Willoughby on the Constitution* (1910), Vol. 1, Sec. 46, pp. 97–98).

As we have already observed, we know of no case which has come before this Court involving a State tax upon the property of an agency such as the Spruce Production Corporation. Several cases have arisen in the courts below, however, and the unanimous opinion of these courts is that such taxation is not valid.

United States v. *Coghlan*, 261 Fed. 425 (District Court of Maryland, Rose, J., Nov. 3, 1919).

King County v. *U. S. Shipping Board Emergency Fleet Corporation*, 282 Fed. 950 (Circuit Court of Appeals, Ninth Circuit, Sept. 5, 1922).

United States Spruce Production Corp. v. *Lincoln County*, 285 Fed. 388 (District Court of Oregon, Dec. 18, 1922).

United States et al v. *Clallam Co.*, 283 Fed. 645 (District Court, Western District of Washington).

These cases are in no wise distinguishable from the case at bar, and the reasoning of the opinions filed fully sustains our present contention. It clearly recognizes that there is a difference in the character of agencies or instrumentalities employed by the Federal Government in the exercise of its constitutional powers; that while it may be true that in the case of an agency not wholly and completely dedicated to the service of the Government a tax upon its property will not interfere with the operations of the Government, nevertheless in the case of a corporation such as the United States Spruce Production Corporation, a tax upon its property is a tax upon the means or instrumentality employed by the Government and is not valid.

The question here is quite different from that decided in *United States* v. *Strang*, 254 U. S. 491, and *Sloan Shipyards* v. *U. S. Fleet Corporation*, 258 U. S. 549. Those cases involved the question whether the Fleet Corporation partook of the sovereignty of the United States to such extent that it possessed that immunity from suit which inheres in the sovereign. Here the question is whether the taxation of the property of the corporation by a State will impose a burden upon the operations of the Federal Government. It would not be contended for a moment that a national bank or a Federal Land Bank is immune from suit, yet it has been held that the franchises of a national bank (*McCulloch* v. *Maryland*, 4 Wheat., 316; *Osborn* v. *United States Bank*, 9 Wheat., 738) and

the essential operations of a Federal Land Bank (*Federal Land Bank of New Orleans* v. *Crossland*, 261 U. S. 374) were immune from taxation by a State.

The Appellants lay great store by the fact (Brief, pp. 26–46) that in the Act providing for the formation of corporations such as the Spruce Production Corporation Congress has not expressly declared that the corporate property shall be free of State taxation. Such declaration, however, is not necessary. There was none in *McCulloch* v. *Maryland*, *Osborn* v. *United States Bank*, *supra*, and other cases which might be cited. The exemption does not depend upon the action or declaration of Congress, but upon the essential necessity of maintaining the operations of the United States free from interference by the States. It is true Congress may waive the immunity, as it has done in the case of real property and shares of stock in national banks. (R. S. §5219.) But it is clear that Congress can not, by its declaration, remove from the taxing power of the States any legitimate subject of State taxation. An express exemption contained in the Act of Congress of July 9, 1918, 40 Stat. 888, c. 143, would stand upon the same footing as those incorporated in the Acts providing for the admission of the several States of the Union and in the Constitutions of the several States. Practically every such Act passed since the admission of Louisiana in 1812, has provided that all real and personal property of the United States shall be exempt from taxation by the State. "Such a provision * * * is not

the foundation of the exemption, but is inserted only from abundant caution, and because the assessment of taxes is to be made by local officers skilled in the valuation of property, but presumably unlearned in legal distinctions." *Van Brocklin* v. *Tennessee*, 117 U. S. 151, 171. So also a declaration of exemption in this case would add nothing, nor does its absence detract.

In considering the attitude of Congress toward corporations of the kind here involved, it is worthy of note that Section 35 of the Criminal Code, as amended Oct. 23, 1918, c. 194, 40 Stat. 1015, now includes "any corporation in which the United States of America is a stockholder." The crimes designated in this section, when committed against such a corporation, are made punishable as crimes against the United States. *United States* v. *Bowman*, 260 U. S. 94.

B.

The property of the Spruce Production Corporation is in fact the property of the United States.

Although it clearly followed from the reasoning of this Court in *McCulloch* v. *Maryland*, *supra*, the principle that property belonging to the United States is not taxable by the States in which it is situated did not receive final judicial affirmation until 1885, in *Van Brocklin* v. *Tennessee*, 117 U. S. 151. The Court there took occasion to make an exhaustive review of the cases touching upon the principle, and in so doing cited with approval several which dealt with the

nature and extent of the interest of the United States in property which is sufficient to remove it from the taxing power of the States (pp. 168–169).

These and later cases make it clear that whether property be exempt from State taxation does not depend upon who holds the legal title nor upon who, in strict technical sense, holds the equitable title, but upon who in fact is the owner for whose benefit the property is held.

Thus where Congress has prescribed the conditions upon which portions of the public domain may be alienated, and these conditions have been met by a prospective vendee but no patent has been issued by the United States, the lands become taxable by the State as the property of the vendee, notwithstanding the legal title remains in the United States.

> *Carroll* v. *Safford*, 3 How. 441.
> *Witherspoon* v. *Duncan*, 4 Wall., 210.
> *Wisconsin Railroad Co.* v. *Price County*, 133 U. S. 496.

And of the lands held in trust for the United States the rule is the same. In *Tucker* v. *Ferguson*, 22 Wallace, 527, in which it was decided that public lands in Michigan, granted by Act of Congress to the State to be held by the State to aid in the construction of a railroad, could not be taxed by the State, Mr. Justice Swayne, delivering judgment, said (p. 572):

> Upon general principles she could not tax the land while the title remained in the United States, nor while she held them as

the trustee of the United States, which, in the view of the law, was the same thing.

But, the Appellants insist, there is no trust involved in the case at bar. (Brief, pp. 46–64.) Extensive research has been made by counsel in an endeavor to prove that the relationship between the Spruce Production Corporation and the United States did not create any trust recognized in law or equity. Whether this be true or not, is not, in our opinion, material to inquire. This Court is not so bound by the form of this transaction that it must be blind to its substance. It is no more obliged to close its eyes to the beneficial interest of the United States in this property than it is to treat as a franchise tax a tax which is essentially a property tax, or to treat as a property tax one which is upon the right of succession.

The corporate form is in this case merely a device by which the United States acquired and held title. It is similar to the situation presented in one of the leading tax cases decided in recent years by the Supreme Court of Pennsylvania. *Commonwealth* v. *Westinghouse Airbrake Co.*, 251 Pa. 12. The Westinghouse Company, for the purpose of conducting its business in Wisconsin and in Canada, had organized corporations under the laws of those jurisdictions and held all of their stock and bonds. It contended that no tax should be paid upon the shares of stock which it held in them for the reason that such shares were merely a means or device by which

it held title to their property, which was located outside the State and beyond its taxing jurisdiction. The contention was sustained. Mr. Justice Elkin said (p. 16):

> The creation of a corporation in Wisconsin and the formation of a limited company in Canada were but a means to an end. It became necessary to do these things in order that the business of the defendant company could be advantageously conducted at those places. To all intent and purposes the defendant company owns these plants just as securely as if the legal title was vested in it. The law regards the substance and not the form, and this is especially true in the construction and administration of taxing statutes: *Western Union Telegraph Co.* v. *Kansas*, 216 U. S. 1. As applied to the facts relating to the Wisconsin and Canadian properties we fully concur in the views expressed by the learned court below. We base our conclusion, as did that court, upon the facts relating to the ownership of these plants.

In principle this case is not unlike those cases in the State courts where, for convenience, a State has created corporate bodies to hold property for and manage public educational and charitable institutions and other governmental projects, and attempts have been made to tax property so held. *Auditor General* v. *Regents*, 83 Mich. 467, 47 N. W. 440, 10 L. R. A. 376; *Tulane* v. *Board*, 38 La. Ann. 296; *Board of Trustees* v. *Champaign County*, 76 Ill. 184;

Reclamation Dist. v. *Sacramento County*, 134 Cal. 477, 66 Pac. 668.

It is true that neither the legal nor equitable title to corporate property is in the stockholders, but it is equally true that the stockholders have a beneficial interest in the property which, in proper cases, is recognized and dealt with by the law.

1 Fletcher Cyc. of Corporations, p. 65.
Frick v. *Webb*, 281 Fed. 407.
Ballaine v. *Alaska Northern Ry. Co.*, 259 Fed. 183.

In a variety of cases it has been held that where the legal fiction of the corporate person stands in the way of substantial justice it will be disregarded.

1 Fletcher Cyc. of Corporations, p. 55.
Chicago, Milwaukee & St. Paul Ry. Co. v. *Minneapolis Civic Assn.*, 247 U. S. 490.
Linn & Lane Lumber Co. v. *United States*, 236 U. S. 574.
McCaskill v. *United States*, 216 U. S. 504, 514.
Cleveland-Cliffs Iron Co. v. *Arctic Iron Co.*, 261 Fed. 15.
United States v. *Beebe*, 127 U. S. 338.

And where this interest is united in a single stockholder, which entirely controls the property and assets of the corporation, the stockholder may be treated as the owner of the corporate property. This identity of ownership is frequently recognized, as the Appellants have pointed out (Brief, pp. 53–54) in cases of fraud, but it is by no means confined to such cases. "The legal fiction of distinct corporate

existence may also be disregarded in a case where a corporation is so organized and controlled, and its affairs are so conducted, as to make it merely an instrumentality, conduit or adjunct of another corporation;" and it is necessary to pierce the veil of corporate existence to do substantial justice. *1 Fletcher Cyclopædia of Corporations*, § 45, p. 63; *Hunter* v. *Baker Motor Vehicle Co.*, 225 Fed. 1006; *Westinghouse Electric. & Mfg. Co.* v. *Allis-Chalmers Co.*, 176 Fed. 362; *Interstate Tel. Co.* v. *Baltimore & O. Tel. Co.*, 51 Fed. 49, aff'd in 54 Fed. 50.

In the case of *United States Grain Corporation* v. *Phillips*, 261 U. S. 106, 113, this Court said: "We must look not at the legal title only but at the facts beneath forms"; and it recognized gold bullion shipped by the Grain Corporation as in substance the property of the United States.

The instant case is one in which the legal forms must be laid aside, and the United States, as the sole stock and bond holder, must be recognized as the owner of the corporate property. When this is done, it is clear that the tax complained against is not valid.

CONCLUSION.

The first question certified—"Did the United States District Court have jurisdiction of the suit?"—should be answered in the affirmative for the reason that (A) the suit has been brought by the United States, and (B) the suit arises under the Constitution of the United States.

The second question—"Is the property held by the Spruce Production Corporation under the above statement of facts subject to State taxation?"—should be answered in the negative, for the reason that (A) the corporation is of such character that taxation of its property is in fact taxation of a means or instrumentality of the Federal Government and imposes a burden upon the United States, and (B) the property of the corporation is in fact the property of the United States.

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SEPTEMBER, 1923.

○ Over

ADDENDUM.

The argument presented herein to sustain immunity of property of the United States Spruce Production Corporation from State taxation, is very strongly supported by the opinion of this court in a case decided since the filing of this brief. (*United States* v. *Leroy W. Walter*, No. 20, October Term, 1923. Opinion delivered by Mr. Justice Holmes, Oct. 22, 1923.)

Congress, recognizing the peculiar interest of the United States in the property of corporations created to serve as governmental instrumentalities in the prosecution of the war, extended the provisions of Section 35 of the Criminal Code so as to punish frauds upon "any corporation in which the United States is a stockholder." (Act of October 23, 1918, c. 194, 40 Stat. 1015.) In the *Walter case*, the defendant was indicted upon three counts; the first two for a violation of this act by a conspiracy to make, present for payment, and obtain payment of a fraudulent claim against a corporation of which the United States owned all the stock. The third, which was based upon the same facts, charged a conspiracy to defraud the United States, in violation of Section 37 of the Criminal Code. All three counts were sustained.

In discussing (in connection with the first two counts) the power of the United States to penalize a fraud upon the corporation, the court said:

> The United States can protect its property by criminal laws, and its constitutional power would not be affected if it saw fit to create a corporation of its own for purposes of the Government, under laws emanating directly or indirectly from itself, and turned the property over to its creature. The creator would not be subordinated to its own machinery.

And as the power of the Government to protect its property by criminal laws is not affected merely because it chooses to hold and use that property through the medium of a corporate form, so also the constitutional immunity from State taxation is not affected.

But the court went further. In sustaining the third count it held that a fraud upon the corporation was a fraud against the United States. Upon this point it was said:

> While it is true that the corporation is not the United States (*United States* v. *Strang*, 254 U. S. 491), the contemplated fraud upon the corporation if successful would have resulted directly in a pecuniary loss to the United States, and even more immediately would have impaired the efficiency of its very important instrument.

In like manner, a State tax imposed upon such a corporation would result directly in pecuniary loss to the United States and would impair the efficiency

of a very important governmental instrument. As the fraud charged in the *Walter case* was a fraud against the United States, so the tax here laid is a tax upon the property of the United States. It is accordingly unconstitutional and void.

Respectfully submitted.

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NOVEMBER, 1923.

WASHINGTON : GOVERNMENT PRINTING OFFICE : 1923

So ordered.

CLALLAM COUNTY, WASHINGTON, ET AL. *v.* UNITED STATES AND UNITED STATES SPRUCE PRODUCTION CORPORATION.

ON CERTIFICATE FROM THE CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT.

No. 255. Argued November 15, 1923.—Decided November 26, 1923.

1. A suit by the United States and its corporate instrumentality against a county and its taxing officers, to avoid state and county taxation of property held by the corporation, upon the ground of

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[1] "If an appeal or writ of error has been or shall be taken to, or issued out of, any circuit court of appeals in a case wherein such appeal or writ of error should have been taken to or issued out of the Supreme Court; or if an appeal or writ of error has been or shall be taken to, or issued out of, the Supreme Court in a case wherein such appeal or writ of error should have been taken to, or issued out of, a circuit court of appeals, such appeal or writ of error shall not for such reason be dismissed, but shall be transferred to the proper court, . . ."

its immunity under the Constitution, is a suit arising under the Constitution, and within the jurisdiction of the District Court. Jud. Code, § 24. P. 344.

2. A State cannot tax the property of a liquidating corporation which, though formed under her laws, was brought into existence and operated by the United States purely as an instrument of war, whose property was furnished, whose stock and bonds are held, and whose assets realized from the liquidation will be taken over, by the United States alone. P. 344. *Thomson* v. *Pacific Railroad*, 9 Wall. 579, distinguished.

QUESTIONS propounded by the Circuit Court of Appeals in a suit brought by the United States and the Spruce Production Corporation to set aside taxes on property held by the corporation. The plaintiffs got a decree in the District Court. 283 Fed. 645.

Mr. Thomas F. Trumbull and *Mr. John D. Fletcher*, with whom *Mr. Overton G. Ellis*, *Mr. Robert E. Evans*, *Mr. William B. Ritchie*, *Mr. F. L. Plummer*, *Mr. John M. Wilson* and *Mr. S. Warburton* were on the brief, for Clallam County et al.

Mr. Solicitor General Beck, with whom *Mr. George Ross Hull*, Special Assistant to the Attorney General, was on the brief, for the United States et al.

MR. JUSTICE HOLMES delivered the opinion of the Court.

This case comes here upon a certificate from the Circuit Court of Appeals. The suit was brought against the appellants, Clallam County, incorporated by the State of Washington, and its taxing officers, for a decree "cancelling", as it is put in the certificate, the taxes levied by the County and State for the years 1919, 1920 and 1921, upon land and other physical property to which the United States Spruce Production Corporation then had the legal title. 283 Fed. 645. The questions certified are (1) whether the District Court of the United States

had jurisdiction of this suit, and (2) whether the property held by the Spruce Production Corporation is subject to state taxation upon facts the statement of which may be abridged as follows.

The Act of July 9, 1918, c. 143, ch. xvi, § 1, 40 Stat. 845, 888, authorized the Director of Aircraft Production to form one or more corporations under the laws of any State for the purchase, production, manufacture and sale of aircraft, or equipment or materials therefor, and to own and operate railroads in connection therewith, whenever in his judgment it would facilitate the production of aircraft, &c., for the United States and Governments allied with it "in the prosecution of the present war." By § 3 within one year from the signing of a treaty of peace with Germany proceedings were to be begun for the dissolution of the corporation so formed. In August, 1918, this corporation was organized under the laws of Washington. The stock except seven shares for the trustees of the corporation was subscribed for by the United States and those shares were controlled by the United States and all property and dividends accruing from them were assigned to the United States. The United States conveyed to the corporation the lands and property now sought to be taxed and a partially performed contract under which these lands were to be acquired and a sawmill and logging railroad were to be built. The corporation issued bonds that were all taken by the United States for cash or in payment for the property conveyed to the company. It proceeded to complete the railroad and mill and to get materials for aircraft for the use of the United States in the war and its activities "were wholly directed to the government's program of production of aeroplane lumber." After the armistice these activities have been directed to liquidating the corporation's affairs, although to accomplish it some further contracts have been made, but, as we understand, solely for that end. The regulations of the Chief of Air

Service appointed under the National Defense Act provide for administrative supervision of the liquidation under the Secretary of War.

In short the Spruce Production Corporation was organized by the United States as an instrumentality for carrying on the war, all its property was conveyed to it by or bought with money coming from the United States and was used by it solely as means to that end, and when the war was over it stopped its work except so far as it found it necessary to go on in order to wind up its affairs. When the winding up is accomplished there will be a loss, but whatever assets may be realized will go to the United States. Upon these facts immunity is claimed from taxation by a State.

The immunity is claimed under the Constitution of the United States. It is true that no specific words forbid the tax, but the prohibition established by *McCulloch* v. *Maryland*, 4 Wheat. 316, was established on the ground that the power to tax assumed by the State was in its nature "repugnant to the constitutional laws of the Union" and therefore was one that under the Constitution the State could not use. 4 Wheat. 425, 426, 430. The immunity is derived from the Constitution in the same sense and upon the same principle that it would be if expressed in so many words. Therefore this suit arises under the Constitution and the District Court had jurisdiction of the case. Judicial Code, March 3, 1911, c. 231, § 24. The first question must be answered, Yes.

The State claims the right to tax on the ground that taxation of the agency may be taxation of the means employed by the government and invalid upon admitted grounds, but that taxation of the property of the agent is not taxation of the means. We agree that it "is not always, or generally, taxation of the means," as said by Chief Justice Chase in *Thomson* v. *Pacific Railroad*, 9 Wall. 579, 591. But it may be, and in our opinion clearly

is when as here not only the agent was created but all the agent's property was acquired and used, for the sole purpose of producing a weapon for the war. This is not like the case of a corporation having its own purposes as well as those of the United States and interested in profit on its own account. The incorporation and formal erection of a new personality was only for the convenience of the United States to carry out its ends. It is unnecessary to consider whether the fact that the United States owned all the stock and furnished all the property to the corporation taken by itself would be enough to bring the case within the policy of the rule that exempts property of the United States. *Van Brocklin* v. *Tennessee*, 117 U. S. 151. It may be that if the United States saw fit to avail itself of machinery furnished by the State it would not escape the tax on that ground alone. But when we add the facts that we have recited we think it too plain for further argument that the tax could not be imposed. See *United States Spruce Production Corporation* v. *Lincoln County*, 285 Fed. 388; *United States* v. *Coghlan*, 261 Fed. 425; *King County* v. *United States Shipping Board Emergency Fleet Corporation*, 282 Fed. 950. We answer the second question, No.

Question 1. Answer, Yes.
Question 2. Answer, No.